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Supreme Court, U.S.
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NO. 88

In The

Supreme Court of the United States

September Term, 1988

CAUCUS DISTRIBUTORS, INC., and CAMPAIGNER PUBLICATIONS, INC., New York Corporations, INDEPENDENT DEMOCRATS FOR LAROUCHE, an unincorporated association, RON FREDMAN, RONALD R. BETTAG, PAUL GREENBERG, and all other parties and organizations acting in concert with the named Petitioners,
Petitioners,

v.

MINNESOTA COMMISSIONER OF COMMERCE,
Respondent.

PETITION FOR WRIT OF CERTIORARI TO THE MINNESOTA COURT OF APPEALS

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QUESTIONS PRESENTED

1. May notes evidencing a loan transaction made to a first amendment political group by a supporter constitute securities under the Minnesota Securities Act?

2. Has the regulation of federal election campaign organizations been preempted by federal law to the extent that the Minnesota Securities Act does not apply to such an organization when a supporter makes a loan in conformity with FEC rules and regulations and receives a promissory note in return?

3. Do the first amendment rights of politically oriented organizations and the individuals who support them prevent a State from using securities law to inhibit the fund raising activities of those organizations?

4. Was the sanction imposed by the Administrative Law Judge precluding Petitioners from contesting the cease and desist order improper in view of Petitioner's first amendment rights?

PARTIES BELOW

The parties in the Minnesota Court of Appeals were Petitioners, Caucus Distributors, Inc., Campaigner Publications, Inc., Independent Democrats for LaRouche, Ron Fredman, Ronald R. Bettag, and Paul Greenberg and all other parties or organizations acting in concert with the above named Petitioners, and Appellee, Minnesota Commissioner of Commerce.

Caucus Distributors, Inc. and Campaign Publications, Inc. are not owned by any parent companies, have no affiliates or non-wholly owned subsidiaries.

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Petitioners,

v.

MINNESOTA COMMISSIONER OF COMMERCE,
Respondent.

PETITION FOR WRIT OF CERTIORARI TO THE MINNESOTA COURT OF APPEALS

Petitioners, Caucus Distributors, Inc., Campaigner Publications, Inc., Independent Democrats for LaRouche, Ron Fredman, Ronald R. Bettag, and Paul Greenberg pray that a Writ of Certiorari issue to review the judgment of the Minnesota Court of Appeals

OPINIONS BELOW

The order of the Minnesota Supreme Court denying Petitioners petition for further review is attached as Appendix A. The opinion and order of the State of Minnesota Court of Appeals is printed as Appendix B. The opinion and order of

the Minnesota Commissioner of Commerce is printed as Appendix C. The Findings of Fact and Conclusions of the Administrative Law Judge are printed as Appendix F-1.

JURISDICTION

The judgment of the Commissioner of Commerce, State of Minnesota was entered September 3, 1987. The judgment of the Court of Appeals of the State of Minnesota was entered March 30, 1988. A timely petition for review of the decision of the Court of Appeals was filed in the State of Minnesota Supreme Court. That petition was denied on June 10, 1988. The jurisdiction of this Court is invoked under 28 U.S.C. Section 1254(1).

STATUTES INVOLVED

Minnesota Securities Act of 1959, Section 80A.14 (Appendix D). Also, Federal Election Campaign Act, 2 U.S.C. 431

STATEMENT OF THE CASE

In December, 1985, the Minnesota Department of Commerce issued an Order for Report of Sales to Caucus Distributors, Inc. (Caucus), a New York non-profit corporation, and/or Campaigner Publications, Inc., also a New York corporation and to Independent Democrats for LaRouche, an unincorporated association and federal political committee recognized by the Federal Election Commission. On February 10, 1986, counsel for Petitioners replied noting they would provide limited information due to the First Amendment nature of the organizations. A second letter was sent by counsel to the Department dated March 6, 1986, which reiterated the First Amendment nature of the organization, provided copies of an acknowledgment of debt and a non-

negotiable document captioned "Unsecured Promissory Note." On behalf of the corporate Petitioners, counsel asserted the First Amendment as a bar to further disclosure concerning the memberships and supporters of the organizations. The correspondence also noted that, based upon the context of the transactions, i.e. loans to political/socio-economic organizations, the loan or loans in question were not securities. Counsel again reiterated this position by letter dated May 22, 1986.

The Department, evidently electing not to pursue resolution of this issue by a Minnesota court, declined to employ the provisions of the Minnesota laws which permits a court to enforce the Order for Report of Sales and Subpoenas by the Department. Minn. Stat. Sec. 80A.20, Subd. 3 (repealed Laws 1987, Ch. 336, effective July 1, 1987).

On June 4, 1986 a Cease and Desist Order was issued by the State of Minnesota, Commissioner of Commerce, along with a Notice of Right of Hearing. On July 17, 1986 an Amended Cease and Desist Order was issued alleging that Petitioners had sold unregistered securities through unlicensed agents in the State of Minnesota.

An initial hearing was held on August 4 and 5, 1986. Because of the 11th hour (July 31) subpoenas by the Department, the hearing was continued after testimony by one witness, Mary Mitchell, who had subscribed to the various publications disseminated by Petitioners, supported many of their political and economic viewpoints and who had also made loans to Petitioners.

The hearing was continued so that the Administrative Law Judge could read various briefs that were to be re-submitted on discovery issues and Petitioners objections to discovery. On October 6, 1986 the Administrative Law Judge reversed an

earlier ruling and issued an Order for Discovery which required organizational Petitioners to provide additional information to the State of Minnesota concerning the identities of persons who had made loans to Petitioner organizations. The Administrative Law Judge did find that Petitioners had shown that their supporters reason to fear disclosure of their identity and the claims of a chilling effect were reasonable and realistic. Petitioners had also pointed out, without success, that the State had never interviewed all of the persons whose names they had been given by Petitioners earlier in the case pursuant to an earlier order. On October 24, 1986 the State moved for an order precluding Petitioners from contesting certain allegations in the amended cease and desist order because it was the State's position that Petitioners had not complied with the Administrative Law Judge's discovery order. On December 2, 1986 the Judge denied the Enforcement Division's request for preclusion. On December 15, 1986 the judge issued another Discovery Order. The Judge directed the organizational Petitioners to provide various information concerning Minnesota residents who had lent money to Petitioners. Since Petitioners had submitted John Doe affidavits from a number of Minnesota citizens requesting anonymity, the Judge asked for a list of all those who had not requested anonymity and of the persons who had requested anonymity, the Judge requested information so that he could randomly select 25% of those who had asked their names not be disclosed (a number of Petitioner's supporters had submitted affidavits alleging fear of retaliation and reprisal if their support for Petitioners became public knowledge) and provide it to the Minnesota Department of Commerce and the Attorney General's office. On December 23, 1986 the Petitioners respectfully declined to disclose any additional names of Minnesota residents who had lent money to Petitioners on First Amendment grounds. Previously, on November 12, 1986 counsel for Petitioners had sent a letter to the Administrative Law Judge advising him that the total number of loans in Minnesota consisted of loans obtained

from 48 people. The Administrative Law Judge was advised that there was some 54 loans altogether, 24 for Campaigner Publications and 30 for Caucus Distributors. On January 13, 1987 the Judge issued an order denying Petitioners request for an interlocutory appeal of his discovery order. On January 27, 1987 the Administrative Law Judge issued an Order Imposing Sanctions for Noncompliance with Discovery on all Petitioners including the individuals. That Order precluded Petitioners from introducing evidence contesting the last sentence of paragraph 1 and paragraphs 2 and 7 of the Department's Amended Cease and Desist Order. The paragraphs in question dealt with the fact that promissory notes were offered or sold to persons in the State of Minnesota and that those promissory notes constituted securities within the meanings of Minnesota State 80(a).14 and, further, that material facts were omitted in the course of obtaining the loans upon which promissory notes were based. The sanction order, for all practical purposes, constituted imposition of a default judgment against Petitioners.

On April 20, 1987, the United States of America filed a petition against Caucus Distributors, Inc. and Campaigner Publications, Inc. seeking to place them in involuntary bankruptcy in the United States District Court for Virginia. Presently, Caucus Distributors, Inc. and Campaigner Publications, Inc. are under the control of interim trustees. A hearing on the bankruptcy issues was scheduled for May, 1988, but as yet no decision rendered.

On July 15, 1987 the Administrative Law Judge issued his Findings of Fact, Conclusions and Recommendations. (Appendix F) On September 3, 1987 the Commissioner of Commerce issued his Findings of Fact and Conclusions of Law and Order (Appendix C), stating that Petitioners shall cease and desist from offering or selling any security or promissory notes or other debt instruments in the State of Minnesota without filing said instrument pursuant to Chapter

80(a) or without obtaining an opinion letter from the Department of Commerce that exempted such instruments. The Department has taken the view that any loan to Petitioners by a Minnesota resident is a security whether or not a note is issued.

On September 9, 1987 Petitioners filed a Petition for Writ of Certiorari in the Court of Appeals. On October 6, 1987 the Writ was granted. On March 30, 1988 the Court of Appeals, State of Minnesota, Judge Randall, issued its decision. The Minnesota Court of Appeals affirmed the Commissioner of Commerce's holdings stating that the promissory notes Petitioners issued constituted securities under Minnesota Statute Section 80A.14; the Federal Election Campaign Act did not preempt regulation of the issuance of securities by Petitioner, Independent Democrats for LaRouche, a federal election campaign committee; Minnesota securities laws as applied to Petitioner's fund raising activities did not impermissibly infringe on Petitioner's first amendment rights of association and the discovery sanctions by the Administrative Law Judge were not an impermissible infringement upon Petitioner's first amendment rights. Petitioners filed a timely petition for further review to the State of Minnesota Supreme Court. This petition was denied on June 10, 1988.

REASONS FOR GRANTING WRIT

I. THE MINNESOTA COURT HAS APPLIED THE MINNESOTA SECURITIES LAW INCORRECTLY AND IN CONFLICT WITH THE FEDERAL CONSTITUTION AND WITH DECISIONS OF THIS COURT.

This case concerns a Cease & Desist Order issued by the State of Minnesota, Department of Commerce, Commissioner of Securities, alleging that Caucus Distributors, Inc., Campaigner Publications, Inc., Independent Democrats for LaRouche, and the individual defendants were selling unregistered securities.

The alleged securities were non-negotiable promissory notes issued by the above organizations acknowledging loans made by political supporters. Caucus Distributors, Inc. is a non-profit New York corporation, Campaigner Publications, Inc. is a New York corporation that effectively operates as a non-profit entity, Independent Democrats for LaRouche is an unincorporated association and political committee recognized by the Federal Election Commission. The individual defendants were volunteers and consultants for the above entities.

These organizations support and disseminate materials that discuss political, social and economic issues of interest to the general public. The State of Minnesota, by its actions in this case, has treated these organizations as business entities ignoring the obvious first amendment goals and aims involved in their activities. This is a case of first impression in Minnesota. The essence of the Minnesota Court's decision is that promissory notes are securities regardless of the first amendment impact of such a decision and the fact that the

Minnesota Statute specifically commands that the context and circumstances of each case be examined in defining a security. This Court has never ruled that promissory notes are always securities within a "plain meaning" approach. See Landreth Timber Company v. Ivan K. Landreth, 471 U.S. 681, 105 S.Ct 2297, 85 L.Ed2d 696 (1985) where this court stated:

> "'Note' may now be viewed as a relatively broad term that encompasses instruments with widely varying characteristics depending on whether issued in a consumer context as commercial paper or in some other investment context. See id., at __. We here expressly leave until another day the question whether 'notes' or 'bonds' or some other category and instrument listed in the definition might be shown by proving 'only' the document itself. (SEC v. C.M. Joiner Leasing Corporation, supra, at 355.) We hold only that 'stock' may be viewed as being in a category by itself for purposes of interpreting the scope of the Act's definition of securities."

The Minnesota Act is substantially similar to the Federal Acts in its definitions. In Section 80A.14 definitions, the Minnesota Act states:

> "When used in Section 80A.01 to 80A.31, the terms defined in this section have the meanings given them unless the context otherwise requires." The Minnesota Act then goes on in Subdivision 18 and defines security as:
>
> "Security (a) "Security" means any note; stock; treasury stock; bond..."

The first amendment impact of the Minnesota Court's decision is great and in effect holds that the State's rights to define what is a security and then to impose a regulation outweighs a substantial, direct and debilitating impact on petitioner's first amendment rights.

The weight of precedent makes it clear that in determining if a promissory note is a security the circumstances and substance of the transaction must be examined. See United Housing Foundation, Inc. v. Forman, 421 U.S. 837, 95 S.Ct 2051, 41 L.Ed2d 621 (1975); SEC v. W.J. Howey Company, 328 U.S. 293, 66 S.Ct 1100, 90 L.Ed 1244 (1946); Marine Bank v. Weaver, 455 U.S. 551, 102 S.Ct 1221, 71 L.Ed2d 409 (1982); and Landreth Timber Company v. Ivan K. Landreth, 471 U.S. 681, 105 S.Ct 2297, 85 L.Ed2d 692 (1985). See also Ansorge v. Kellog, MI Ct. of App. (1988) (Appendix H); No. 86910 and Froelich v. Caucus Distributors, Inc., Ill Cty Cir. Ct., No. 86L17562 (1988). (Appendix G).

In this case the petitioners argue that the first amendment aspects of the Petitioner organizations are among those circumstances and must be weighed with great deference in the initial determination of whether or not a security is involved in the transaction in question. The ruling by the Minnesota Court of Appeals is wrong because it classified the promissory notes in this case as securities without regard to the first amendment purpose of the Petitioners and the first amendment nature of the fund raising activity being conducted.

The State of Minnesota has tried to treat these loan transactions as if they were investments as that term is used in the context of a security. An examination of the context of the loans makes the first amendment concerns very clear. The appellant organizations do not make or distribute profits, workers are paid minimum amounts or are volunteers. The money received by the organizations are spent disseminating books, pamphlets, newspapers and other materials that discuss issues seen as important to society and the voters.

In examining the context of these transactions the State must regulate carefully with appropriate deference to the first amendment. See In re Primus, 436 U.S. 412 (1978).

> "Where political expression or association is at issue, this court has not tolerated the degree of imprecision that often characterizes govern ment regulation of the conduct of commercial affairs. The approach we adopt today in Ohralik posts, p.447, 56 L.Ed2d 444, 98 S.Ct 1912, that the state may proscribe in person solicitation for pecuniary gain under circumstances likely to result in adverse consequences cannot be applied to appellant's activity on behalf of the ACLU." at 437.

The Minnesota Court of Appeals stated in its opinion that Petitioners were not engaging in first amendment activity in seeking loans. Fund raising is vital to a political party or organization, particularly a small one. In the case of Federal Election Campaign Committee v. Hall-Tyner Election Campaign Committee, 678 F.2d 416 (1982, 2 Nd Cir.), Judge Kaufman stated:

> "Acknowledging the importance of fostering the existence of minority political parties, we must also recognize that such groups rarely have a firm financial foundation. If apprehension is bred in the mind of contributors to fringe organization by fear that their support of an unpopular ideology will be revealed, they may cease to provide financial assistance. The resulting decrease in contribution may threat the minority parties very existence. Society suffers from such a consequence because the free flow of ideas, the life blood of the bodily politic, is necessarilly reduced. Accordingly, a nation dedicated to free thought, free expression cannot ignore the grave results of facially innocuous election requirements."

This is exactly the situation in the instant case. Petitioners assert that it is not enough in this case to decide, as the lower

court did, that the notes are securities and then hold that the State has a compelling interest in regulating securities. Therefore, Petitioners first amendment interest are overcome. It is the position of Petitioners that the first amendment interest must be considered in determining if there is, in fact, a security involved in the transaction. This is "the context" in which the transaction took place. Petitioners concede that the State has an interest in regulating the sale of securities. Petitioners point is that in the context of this case, these notes are being used to raise funds in connection with a political first amendment purpose and, therefore, should not be considered securities in the first place.

Further, it is apparent that if notes issued in the context of this case are considered securities no political organization could ever comply with the required reporting and disclosure requirements of a State's Securities Act. Almost all the State's Securities Acts are based on the Uniform Securities Act and require that the organizations issuing securities fit criteria which are completely unrealistic when applied to a political organization. Political organizations usually do not have large capital assets and they do not tend to accumulate capital. Political organizations do continuous fund raising and most State's registration requirements would demand that they set specific times to begin and end fund raising. Political and first amendment associational organizations differ even from religious organizations in that they do not, as a rule, accumulate large items of property or large asset bases.

These organizations would not be able to overcome the problems presented by state rules which have restrictions on fund use, required statutory earnings, minimum capitalizations, and strict rules concerning distribution of non-factual or inaccurate material. Obviously, many claims made in the course of a political campaign do not turn out to be factual. Some 28 states have merit review which gives too much discretion to the Commissioner of Securities in that State

concerning registration. In other words, these commissioners who are political appointees could determine a loan to a political group was not a good investment. There are no criteria for what a "good" investment is.

Moreover, treating political loans as securities requires all fund raisers to be licensed securities agents working for licensed securities brokers. Brokers and their agents are required, in Minnesota and most other states, to maintain lists of all "sales" and make them available for inspection by the Securities Commissioner and to determine if the investment is "suitable" for the "buyer". Thus, if one is well to do, one may support a political organization that is "risky" or not a traditional mainstream Republican or Democratic group. If too old, too young or not wealthy enough, the "investment" would likely be found "unsuitable". Those who wished to support a political group in this manner could not do so with anonymity. Supporters who wished to fund raise would have to pass examinations on securities laws to obtain agents licenses, i.e. face "super literacy" tests more onerous than those employed in the past to suppress racial and ethnic minorities. As noted in Petitioner's appeals briefs, the list of debilitating impairments goes on and on.

When one thinks of the concept of material disclosure under the securities laws being applied to political candidates, the mind boggles. Would a candidate have to disclose an extra marital affair if it might impact the success of his campaign? Would it be a material misstatement to claim the candidate would defeat his opponent if that was unlikely. The ramifications of applying securities concepts to first amendment organizations and political campaigns are staggering in their potential impact to core first amendment rights.

The first amendment aspects of this case allow for an analogy to be drawn from a recent Supreme Court decision which, although it did not deal with securities regulation, found that a section of the Federal Election Campaign Act was unconstitutional under certain circumstances. The case in question was the Federal Election Commission v. Massachusetts Citizens for Life, Inc., 107 S.Ct 616, 93 L.Ed2d 539, 55 U.S. LW 4067. This case concerned Section 316 of the Federal Election Campaign Act which prohibited corporations from using treasury funds to make an expenditure in connection with any election to any public office and required that any expenditure for such purpose be financed by voluntary contributions to a separate fund.Massachusetts Citizens for Life, like petitioners, was a non-profit, non-stock corporation. Its purpose was to foster respect for human life and defend the right to life of all human beings born and unborn through educational, political or other forms of activities (one of the goals of Petitioners herein). To further this activity it published newsletters that had been distributed to contributors and to non-contributors who expressed support for the organization. This court stated that the concern underlined in the regulation of corporate political activity - that organizations that amass great wealth in the economic marketplace not gain unfair advantage in the political marketplace - was absent with regard to Massachusetts Citizens for Life. The court opined:

> "This rationale for regulation is not compelling with respect to independent expenditures by appellee. Individuals who contribute to appellee are fully aware of its political purposes and, in fact, contribute precisely because they support those purposes. It is true that contributors may not be aware of the exact use to which his or her money ultimately may put or the specific candidate used to support. However, individuals contribute to a political organization as a more effective means of advocacy than spending money under their own direction..." at 4073.

Recently, this Court decided a similar situation involving a State's overprotective attitude towards its citizens. In the case of Meyer v. Grant, 108 S.Ct 1886 (1988), the State of Colorado had forbidden paid solicitors from circulating political petitions. The State's logic was that such paid solicitors would have more reason to falsify signatures. This Court held that such a ban was an infringement on the first amendment rights of citizens wishing to bring political questions in front of the voters. This Court stated:

> "We agree with the Court of Appeals conclusion that the statute trenches upon an area in which the importance of the first amendment protections is 'at its zenith'. For that reason, the burden that Colorado must overcome to justify this criminal law is well nigh insurmountable." at pg. 1894.

Petitioners in this case would make the same claim that because of the nature of their organizations and the purposes of those organizations that the first amendment protection in this case is at its highest and the State's actions are subject to exacting scrutiny.

As is apparent from the letter made part of the record in this case sent out by the Attorney General for the State of Minnesota, the ideas and beliefs of the Petitioner organizations and Lyndon LaRouche are not popular with the Minnesota Attorney General. He stated: "We must show the Nation that Minnesota will not tolerate the LaRouche fringe." Nor do Petitioners seem to be popular with other states. Notwithstanding that this securities issue is one of first impression, supporters and fund raisers have been charged with felony security law violations in Virginia, Missouri and New York. However, the use of the securities law to censor those ideas is improper. As this Court stated in NAACP v. Button, 371 U.S. 415, 83 S.Ct 328, 9 L.Ed2d 405 (1963):

> "The First Amendment is a value free provision whose protection is not dependent on the truth, popularity, or social utility of the ideas and beliefs which are offered."

It should be noted that supporters dissatisfied with repayment of their loans have other remedies available under Minnesota law. There are consumer protection statutes enforceable by the Attorney General and individuals, common law fraud causes of action, criminal fraud statutes and actions in debt available to aggrieved persons.

II. THE MINNESOTA COURT OF APPEALS HAS IMPROPERLY APPLIED MINNESOTA SECURITIES LAW TO INDEPENDENT DEMOCRATS FOR LAROUCHE, A CAMPAIGN ORGANIZATION REGULATED UNDER THE FEDERAL ELECTION COMMISSION IN CONFLICT WITH THE DECISIONS OF THIS COURT.

Respondent Independent Democrats for LaRouche's (IDL) loans should not fall within the purview of the Minnesota Securities Act because this organization was a campaign organization formed to aid Lyndon LaRouche in his campaign for the presidency of the United States. The Federal Election Campaign Act amendments of 1974 are an attempt by Congress to reform campaign expenditures and political contributions. This Act evidences a clear intent to preempt any State law regarding campaign expenditures and political contributions. To use the Minnesota Securities Law against Independent Democrats for LaRouche effectively circumvents the Federal Election scheme.

The Supreme Court outlined the various facts of federal preemption law in Louisiana Public Service Commission v. F.C.C., 106 S.Ct 1980, 1898-99 (1986):

> "The Supremacy Clause of Art. VI of the Constitution provides Congress with the power to preempt state law. Preemption occurs when Congress, in enacting a federal statute, expresses a clear intent to preempt state law, Jones v. Roth Packing Co, 430 U.S. 519, 97 S.Ct 1305, 51 L.Ed.2d 604 (1977), when there is outright or actual conflict between federal and state law, e.g., Free v. Bland, 369 U.S. 663, 82 S.Ct 1089, 8 L.Ed.2d 180 (1962), where compliance with both federal and state law is in effect physically impossible, Florida Lime & Avocado Growers, Inc. v. Paul, 373 U.S. 132, 83 S.Ct 1210, 10 L.Ed.2d 248 (1963), where there is implicit in federal law a barrier to state regulation, Shaw v. Delta Air Lines, Inc., 463 U.S. 85 103 S.Ct 2890, 77 L.Ed.2d 490 (1983), where Congress has legislated comprehensively, thus, occupying an entire field of regulation and leaving no room for the states to supplement federal law, Rice v. Sante Fe Elevator Corp., 331 U.S. 218, 67 S.Ct 1146, 91 L.Ed. 1447 (1947), or where the state law stands as an obstacle to the accomplishment and execution of the full objectives of Congress. Hines v. Davidwitz, 312 U.S. 52, 61 S.Ct 399 85 L.Ed. 581 (1941). Preemption may result not only from action taken by Congress itself; a federal agency acting within the scope of its congressionally delegated authority may preempt state regulation. Fidelity Federal Savings & Loan Assn. v. De la Cuesta, 458 U.S. 141, 102 S.Ct 3014, 73 L.Ed.2d 664 (1982); Capital Cities Cable, Inc. v. Crisp, 467 U.S. 691 (1984)."

The Federal Election Campaign Act Amendments of 1974 present an express preemption issue. As the Supreme Court stated in Silkwood v. Kerr-McGee Corp., 104 S.Ct 615, 621 (1984): "if Congress evidences an intent to occupy a given field, any state law falling within that field is preempted."

Further, when a federal statute unambiguously preempts certain state legislation, the statutory language is controlling and preemption takes place. Exxon Corp. v. Hunt, 106 S.Ct 1103, 1109 (1986); Aloha Airlines, Inc. v. Director of Taxation, 464 U.S. 7, 12 (1983).

The Federal Election Campaign Act Amendments of 1974, public law 93-443, 88 Stat. 1263, reprinted in 1974 U.S. Code Congressional and Administrative News, p. 1436, et. seq., contain three different provisions regarding preemption of state law. The first provision is contained in Section 104 of the Act. Section 104 reads as follows:

> "Sec. 104
> (a) The provisions of Chapter 29 of Title 18 United States Code, relating to elections and political activities, supersede and preempt any provision of state law with respect to election of federal office.
>
> (b) For purposes of this section, the terms "election", "federal office", and "state" have the meanings given them by section 591 of Title 18 United States Code."

The legislative history explaining this provision states:

> "Conference Substitute - The conference substitute is the same as the House amendment. The provisions of the conference substitute make it clear that the federal law occupies the field with respect to criminal sanctions relating to limitations on campaign expenditures, the sources of campaign funds used in federal races, the conduct of federal campaigns, and similar offenses, but does not affect the state's rights to prohibit false registration, voting fraud, theft of ballots, and similar offenses under state law."

Senate Report no. 93-689, reprinted in 1974 U.S. Code Congressional and Administrative News 5587, 5638.

There is a second preempting provision. Section 301 of the Federal Election Campaign Act Amendments of 1974, codified at 2 U.S.C. Section 453 provides:

> "The provisions of this Act, and of rules prescribed under this Act, supersede and preempt any provision of state law with respect to election to federal office."

This is very broad language. Its breadth is confirmed by the legislative history. The legislative history concerning this section of the law states:

> "Senate Bill:
> Section 213 of the Senate bill amended Section 403 of the Act, relating to effects on state law, to provide that the provisions of the Act preempt any provision of state law with respect to campaign for election to federal office.
>
> House Amendment:
> Section 301 of the House amendment amended Section 403 of the Act, relating to effect on state law, in essentially the same manner as the amendment made by Section 213 of the Senate Bill.
>
> Conference substitute:
> The conference substitute follows the House amendment. It is clear that the federal law occupies the field with respect to reporting and disclosure of political contributions to and expenditures by federal candidates and political committees, but does not affect state laws as to the manner of qualifying as a candidate, or the dates and places of elections."

Senate report #93-689, reprinted at 1974 U.S. Code Congressional and Administrative News 5587, 5668.

Both the plain meaning of the statute and the legislative history makes Congress' intent to preempt very clear. As

noted above, in such a case, preemption must be deemed to occur.

An attempt by the State of Minnesota to use their securities law to regulate an organization such as IDL which was formed to deal with the election of an individual to federal office, is a use of the law directly in contradiction to the Federal Act. The hearings officer in this matter has attempted to rule that the federal preemption only applies to election laws. The Federal Act specifically regulates loans to campaign committees. 2 U.S.C. Section 431(8); 11 CFR Section 100.7. Clearly, under these circumstances, the Minnesota Securities Act is operating as an election law and addresses an area specifically regulated by the Federal Act.

III. THE SANCTION IMPOSED BY THE ADMINISTRATIVE LAW JUDGE PRECLUDED THE PETITIONERS FROM CONTESTING A CEASE AND DESIST ORDER AND WAS IMPROPER IN THAT IT DEPRIVED PETITIONERS OF A FAIR AND IMPARTIAL HEARING AND INFRINGED UPON THEIR FIRST AMENDMENT RIGHTS.

On January 27, 1987 the Administrative Law Judge issued an order precluding Petitioners from introducing evidence contesting the last sentence of paragraphs 1, 2 and 7 of the State's Amended Cease and Desist Order. Paragraph 2 was the ultimate issue of the contested case in that it alleged that the promissory notes offered by Petitioners constituted securities within the meaning of the Minnesota Securities Act. Thus, Appellants were not able to present witnesses or evidence at a hearing to contest the State's allegations that the transactions involved in this matter constituted a sale of securities. The sanction order was based on the fact that the corporate

Petitioners had resisted throughout the course of the proceeding the States attempts to obtain a list of Petitioner's supporters, contributors and lenders. Petitioners resisted these attempts on the part of the State on first amendment and privacy grounds. Petitioners contended that the orders and subpoenas of the Minnesota Division of Securities inhibited Petitioners and their supporters respective rights of association, belief and freedom of speech as guaranteed by the United States Constitution under the First and Fourteenth Amendments. Further, Petitioners contended that supporters and contributors right of privacy under the United States and Minnesota Constitutions were being violated. Petitioners submitted John Doe and other affidavits from or addressing approximately 19 persons who had made loans to Petitioner's organizations. These affidavits indicated that these lenders and supporters did not wish their names revealed to government agencies for fear of harassment or retaliation. In the October 6th discovery order, the Administrative Law Judge recognized this fear on the part of Petitioner's supporters and acknowledged that a chilling effect caused by this fear was probable. At the beginning of the case, Petitioners had revealed seven names to the State (with the permission of those supporters) and the State had not even taken the trouble to interview all of those individuals.

First amendment rights are to be interpreted liberally. They are fundamental and occupy a preferred place in society. As this Court stated in NAACP v. Alabama, 357 U.S. 449, 78 S.Ct 1163, 2 L.Ed2d 1488 (1958):

> "Inviobility of privacy in group association may in many circumstances be indispensable to preservation of freedom of association, particularly where a group espouses dissident beliefs." at page 462.

There is no doubt that the overwhelming weight of authorities is to the effect that forced disclosure of first

amendment activities creates a chilling effect which must be balanced against the State's interest in obtaining that information. Australia/Eastern U.S.A. Shipping Conference v. U.S., 537 F.Supp 807 (1982). The State of Minnesota had received some seven names from Petitioners and had not bothered to contact even all of those individuals to make its case. Further, the State attempted to argue that a list of all Petitioner's supporters and lenders was needed in order to determine whether Petitioners could claim a limited offering exemption. Petitioners at all times during this case made it clear to the State that it did not wish to claim a limited offering exemption. The State's interest could not be compelling under these circumstances.

In the case of Federal Election Commission v. Hall-Tyner Election Campaign Committee, 678 F.2d 416 (2nd Cir., 1982), Judge Kaufman stated:

> "Anonymity has long been essential to uninhibited political activity in a democratic society. The secret ballot insures that no one must answer for the vote he cast. Confidentiality prevents the apprehension of reprisal that threatens to suppress the robust interchange of ideas at the core of the First Amendment's guarantee of free speech and protection of privacy and association. A society confident in its stability does not fear the voice of opposition. Indeed, unafraid of dissent, we recognize our ability to exhibit special indulgence to nurture the free expression of minority views. Realizing that mere identification with certain disfavored ideologies can result in harassment which may silence those voices, the Constitution protects private support of political associations."

Also,

> "Acknowledging the importance of fostering the existence of minority political parties, we must also recognize that such groups rarely have a firm financial foundation. If apprehension is bred in the mind of

> contributors to fringe organizations by fear that their support of an unpopular ideology will be revealed, they may cease to provide financial assistance. The resulting decrease in contributions may threaten the minority parties very existence. Society suffers from such a consequence because the free flow of ideas, the life blood of the body politic, is necesarily reduced. Accordingly, a nation dedicated to free thought and free expression cannot ignore the grave results of facially innocuous election requirements.
>
> The power of the government to repress dissent is substantial and can be exercised in a myriad of subtle ways. Privacy is an essential element of the right of association and the ability to express dissent effectively. As a result, removing the cloak of anonymity from a political committee by requiring it to disclose the names of those who purchase its publications, threatens important first amendment values. Such forced revelations would likely lead to 'vexatious inquiries' which consequently could instill in the public an unremitting fear of becoming linked with the unpopular or the unorthodox."

The view of the Minnesota Attorney General's Office concerning organizations associated actually or reputedly with Lyndon LaRouche is illustrated by the attached Appendix I. The State in this case had sufficient facts available through the testimony of parties to the transactions at issue and would have had further facts available had it taken the trouble to interview all seven of the people whose names were given to them by Petitioners. The further discovery of contributors and lenders was merely official curiosity and would expose Petitioner's sympathizers unnecessarily.

It is clear that in a situation such as this Petitioners could not comply with the State's discovery orders without waiving important constitutional rights. Such a refusal by Petitioners is not willful, nor is it done in bad faith. See Edgar v. Slaughter, 548 F.2d 770 (8th Cir., 1977) and Socite Internationale v.

Rogers, 357 U.S. 197, 78 S.Ct 1087, 2L.Ed2d, 1255 (1958). Petitioners even requested an interlocutory appeal. The State of Minnesota decisions have consistently held the factors to be considered in a sanctions manner are (1) the wilfullness of the failure to disclose; (2) the resulting prejudice; and (3) the harm to the truth seeking process if severe sanctions are imposed. Cornfeldt v. Tongen, 262 N.W.2d 684 (1977). It is clear in this case that the Petitioners tried to comply with the State's orders as best they could and still be consistent with the constitutional restraints they felt were present. Further, the harm imposed by the sanction was great. It, in effect, deprived Petitioners of the ability to present their case in front of the Hearings Officer. The State of Minnesota was in no way prejudiced by Petitioner's failure to reveal all of the names.

CONCLUSION

This writ request should be granted because this case presents a classic constitutional confrontation between the core freedom of individuals and groups whose viewpoints are not traditional and the more traditional mainstream political governmental authorities seeking to suppress dissident viewpoints. Treating loans to political associations as securities opens a veritable pandora's box of debilitating blows to the sanctity of the First Amendment. Numerous less restrictive alternatives are available to police areas of legitimate concern. These alternatives include a variety of civil and criminal remedies which do not intrude on the First Amendment yet effectively and fully address state interests. See Meyer v. Grant, 108 S.Ct 1886, 56 USLW 5616 (1988).

Permitting the states (there are 14 states with cease and desist orders pending against some or all of Petitioners) to impose securities regulation requirements on political associations and federal campaign committees creates an impermissible opportunity for of politically motivated suppression of both dissident and opposing political viewpoints. While efforts of securities commissioners are

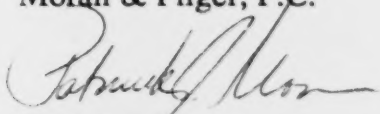
confined to suppressing these Petitioners at the moment, history demonstrates that the temptation to use this power will prove irresistible. The practice will spread if not ended now.

In this day and age, fund raising is critical to effective dissemination of viewpoints. Publication of newspapers, magazines, books and flyers on a national basis is expensive. Use of loans is a traditional method of political fund raising. That is why it was addressed by the Federal Act and by Federal Election Commission regulations. If it is a "security" for these Petitioners, it is one for all campaign committees. A loan could not issue unless registered as a security. A loan could only be solicited by a licensed agent who worked under the supervision of a licensed broker. If fund raising exceeded certain limits ($100,000 to $500,000), a prospectus or offering memorandum would be required in many states. The devastating impact of this ruling in the Minnesota Supreme Court is likely to be followed in Alaska, Maryland, Washington, Virginia, Missouri, Indiana, Illinois, New York, Massachusetts and elsewhere. There is a clear need to address this issue now.

The granting of this writ would be an important step towards clarifying the law as to the circumstances under which promissory notes constitute securities subject to regulation under state or federal securities acts.

Respectfully submitted,

Moran & Pilger, P.C.



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APPENDIX

STATE OF MINNESOTA

IN SUPREME COURT

C4-87-1952

Caucus Distributors, Inc., et al.,

Relators,

vs.

Commissioner of Commerce,

Respondent.

ORDER

Based upon all the files, records adn proceedings herein, It is hereby ordered that the petition of Caucus Distributors, Inc., Campaigner Publications, Inc. and Independent Democrats for La Rouche for further review be, and the same is, denied.

Dated 6-10-88

By the Court

(signed)

Chief Justice

STATE OF MINNESOTA
DEPARTMENT OF COMMERCE
COMMISSIONER OF COMMERCE

In the Matter of Caucus
Distributors, Inc., and
Campaigner Publications, Inc.,
New York Corporations, Independent
Democrats for LaRouche, an Unincorporated
Association, Ron Fredman, Ronald R. Bettag,
Paul Greenberg, and All Other Parties and
Organizations Acting in Concert with the
Named Respondent.

FINDINGS OF FACT, CONCLUSION OF LAW, AND ORDER

COM/S-86-047-JL
8-1005-698-2

The above-entitled matter came on for hearing before Administrative Law Judge Jon Lunde, on Monday, August 4, 1986 at the Office of Administrative Hearings in Minneapolis, Minnesota. Additional proceedings were held the following day. The hearings were held pursuant to an Order for Hearing, an Order Suspending Exemption issued by the undersigned on June 4, 1986, and an amended Cease and Desist Order, Notice of Right to Hearing and Order Suspending Exemption issued by Deputy Commissioner of Commerce James Miller on July 17, 1986.

Jerome Getz, Special Assistant Attorney General, 1100 Bremer Tower, Seventh Place and Minnesota Street, St. Paul,

Minnesota 55101, appeared on behalf of the Minnesota Department of Commerce (Department). Patrick Moran, Moran & Pilger, P.A., Attorneys at Law, 1221 Lamar Building, Suite 517, Houston, Texas 77010, appeared on behalf of each of the above-named organizations and individuals. The record closed on May 20, 1987.
Thereafter, on July 15, 1987 Administrative Law Judge Lunde issued his Findings of Fact, Conclusions and Recommendations to the undersigned. On July 20, 1987, the undersigned sent notice that exceptions and arguments should be filed with the Department of Commerce no later than August 12, 1987, and the Attorney General filed exceptions and argument on August 14, 1987.

Based upon an examination of the transcript and exhibits, and upon a review of all the briefs and all of the other records, files and proceedings herein, the undersigned makes the following:

FINDINGS OF FACT

1. Caucus Distributors, Inc., (Caucus) is a Not-For-Profit corporation incorporated under the laws of the State of New York. The Certificate of Incorporations its incorporators filed with the New York Department of State on April 5, 1982 reads in part as follows:

* * *

2. The corporation * * * is not formed for pecuniary profit or financial gain, [and] * * * no part of the assets, income or profit of the corporation is distributable to, or inures to the benefit of its members, directors or officers or any private person except to the extent permissible under the Not-For-Profit Corporation Law.

3. The purposes for which the corporation is formed are:

> To promote and encourage the political and [sic] ideas and beliefs fostered by the International Caucus of Labor Committees and other organizations advocating the same ideas and beliefs; to distribute to the general public, sell and obtain subscriptions to publications specifically dedicated to the political ideas and beliefs fostered by the International Caucus of Labor Committees and other organizations; to solicit membership for certain membership organizations associated with the publications distributed by the corporation consonant with the goals, purposes and programs of those organizations; to advertise and promote the publications distributed by the corporation; to engage the services of writers, reporters, editors, distributors, corporations, associations, partnerships and new agencies in furtherance of these purposes; ***

2. Campaigner Publications, Inc. (Campaigner) is a New York corporation.

3. Independent Democrats for LaRouche (IDL) is an unincorporated association and a political committee apparently recognized by the Federal Election Commission. Paul Greenberg is an authorized representative of IDL and is empowered to sign notes on its behalf.

4. At all times material to this case, Ron Fredman and Ronald R. Bettag worked for Caucus and solicited loans to Caucus, IDL and Campaigner by selling notes for them.

5. Ron Fredman, Ronald R. Bettag and Paul Greenberg are not and have never been licensed by the Department to sell

securities in the State of Minnesota. Likewise, Caucus, Campaigner, and IDL are not and never have been licensed by the Department to sell securities in the State of Minnesota.

6. Mary M. Mitchell, an 85-year-old widow, is a resident of Minneapolis, Minnesota. She has lived there since moving from Winona in 1938. Mitchell is a retired stenographer who has a high school education.

7. In July, 1984, while walking on the Mall near.Seventh and Nicollet in downtown Minneapolis, Mitchell was given a pamphlet pertaining to the presidential candidacy of Lyndon LaRouche. She told the man who gave her the pamphlet that she had seen LaRouche on television and liked what she saw. The man told her that if she gave him her name and telephone number someone would call her with more information about LaRouche. She gave him the information.

8. Approximately one week after her encounter on the Mall, Ron Fredman telephoned Mitchell from Chicago to talk to her about LaRouche, Caucus, Campaigner and IDL. Fredman told Mitchell about corruption in the world and the need for Americans to clean it up. He specifically mentioned drug trafficking in the Middle East and South America, the laundering of Mafia money by banks, the decline in American culture, and bank failures. He told Mitchell that some banks were shaky and that if the United States didn't pull together, everyone would go bankrupt. Fredman told Mitchell that LaRouche needed her help with these problems and he asked her for a contribution. She agreed to make a $25 contribution at that time, and he made arrangements for her to receive copies of "New Solidarity" and other publications.

9. During that initial telephone conversation, Fredman also asked Mitchell to help by making loans. Fredman told her

that she would receive a promissory note for any loans she made and that she could specify the interest rate and the term of the notes. Since she would get a promissory note and could specify the interest rate, Mitchell concluded that the loans would be similar to a banking transaction. Moreover, since LaRouche was "in the limelight", she concluded that she was not dealing with a fly-by-night operation that would skip the country, and that her loans would be a good investment. Therefore, she agreed to make a $15,000 loan at that time. In return, she was to receive two notes payable at the end of three years. One was to be made payable to her and her stepson, R. Keith Mitchell, in the principal amount of $10,000. The other was to be made payable to her and her sister-in-law, Mozell Hall, in the principal amount of $5,000. Fredman personally collected two checks in the aggregate amount of $15,000 from Mitchell at her home in Minneapolis early in July 1984. Later that month, two promissory notes were mailed to her in the aggregate principal sum of $15,000. The notes stated the payees, amounts, term and interest rate Fredman promised.

10. On September 3, 1984, Fredman called Mitchell again and asked her to loan $1,000 to IDL. She agreed to make a $1,000 loan to IDL for one year at ten percent interest. Following her conversation with Fredman, she mailed him a $1,000 check payable to IDL's order. A few days later, she received a promissory note signed by Paul Greenberg, as an authorized representative of IDL. The note was in the principal sum of $1,000, bore interest at the rate of ten percent, and was payable in one year. The note, and accumulated interest thereon, was paid by IDL in July 1986.

11. On or about September 17, 1984, Fredman telephoned Mitchell again to give her an update on the activities of the LaRouche organizations. At that time, he gave her more information on their efforts to eliminate drug traffic and related activities in the Middle East. In addition, he talked about a publication entitled "Dope, Incorporated" which one of the

organizational Respondents had published. During that telephone conversation, Mitchell agreed to make an additional $5,000 loan to Caucus for 90 days with interest at 15 percent. Immediately after her telephone conversation with Fredman, Mitchell mailed him a check payable to Caucus in that amount. A few days later, Mitchell received Caucus' promissory note incorporating the loan terms she and Fredman had discussed.

12. On or about November 26, 1984, Fredman called Mitchell to solicit another loan. During that conversation, Mitchell expressed regret for having made the initial $15,000 loan for a term of three years. He told her that if she returned the notes to him, he would issue two new notes which would mature in a year (on November 26, 1985). At that time, Fredman persuaded Mitchell to make an additional $10,000 loan to Caucus for six months. When Mitchell told Fredman she was getting 14 percent on a certificate of deposit with her bank, he said that Caucus would pay 16 percent on the loan.

13. On or about November 26, 1984, a $10,000 promissory note signed by Fredman for Caucus was mailed to Mitchell. It reflected a six-month term and a 16 percent interest rate as she and Fredman had agreed on November 26. At the same time, Mitchell was mailed two promissory notes replacing those which she had returned due to her dissatisfaction with their three-year maturity date. Exhibits 19 and 23. Those notes were signed by Fredman and Campaigner and reflected a one-year term and a 12 percent interest rate. The payees were the same as those in the notes originally issued.

14. Caucus' September 17, 1984 note -or $5,000 was due on December 17, 1984. On or about the due date, Fredman called Mitchell and told her that the note could not be paid because their assets had been frozen by a bank, and he asked her if she would accept a one-third partial payment. Although

Mitchell agreed that the bank's explanation for freezing Caucus' funds was "outlandish", she said she would like half of the note paid. Fredman said he would see if that could be done and call her back. Early in January, 1985, after Mitchell returned from a vacation, Fredman called her and asked if she would accept a new note covering Caucus' $5,000 loan to be payable in five monthly principal installments of $1,000 commencing May 1, 1985 and a lump sum interest payment on October 1, 1985. She agreed and a short time later received a promissory note from Caucus in the principal sum of $5,000. Exhibit 7. That note contained the payment terms she had agreed to accept and was signed by Fredman for Caucus.

15. In April 1985, Mitchell asked Fredman if the beneficiaries on Campaigner's November 26, 1984 notes could be changed. He said that could be done and they agreed that Campaigner's two notes (Exhibits 19 and 23) would be destroyed and that one new note would be issued in the principal amount of $15,000. Mitchell also agreed that the rate of interest could be reduced from 12 percent to 10 percent on the new note. Exhibit A. A short time later, a $15,000 note payable in one year with interests at 10 percent was mailed to her. Exhibit 24. Caucus was listed as the payor of that note and it was signed by Fredman. The note was dated April 16, 1985 rather than November 16, 1984. Mitchell did receive interest on the $15,000 loan between November 26, 1984 and April 16, 1985, did not agree to waive interest earned during that time, and did not authorize a change in the date of the two notes when they were rolled over and consolidated.

16. During the telephone conversation between Mitchell and Fredman on April 10, 1985, Mitchell agreed to make an additional loan to Caucus in the amount of $10,000. The loan was made in two separate payments to Caucus. A $6,000 payment was made by a check dated April 10, 1985 and a $4,000 payment was made to Caucus by a check dated April 26, 1985. On or about April 29, 1985, Caucus' $10,000

promissory note was mailed to Mitchell. The note, which was signed by Fredman, carried an interest rate of 10 percent and was payable in six months.

17. Apart from her loan to IDL, Mitchell loaned $40,000 to Caucus between July 1984 and April 29, 1985. As of November 21, 1985, only $2,000 had been repaid to her. A $1,000 payment was made late in April 1985, a $500 payment was made on November 6, 1985 and a $500 payment was made on September 30, 1985 (two checks).

18. During their telephone conversation in 1984 and 1985, Mitchell and Fredman primarily talked about Caucus, but he never explained his relationship to Caucus, Campaigner or IDL. In addition, he never told her how they would repay the loans, if they had solicited loans from other persons, or if they had repaid those loans in a timely fashion.

19. All of Mitchell's loans to the Respondents, except the $1,000 loan made to IDL, were made by check payable to Caucus. All the checks were presented for payment and paid by her bank. Mitchell did receive interest on the $15,000 loan between November 26, 1984 and April 16, 1985, did not agree to waive interest earned during that time, and did not authorize a change in the date of the two notes when they were rolled over and consolidated. All the loans we:- solicited by Fredman. Mitchell had no direct contact with Greenberg and had very limited contact with Bettag. Her only contact with Bettag occurred in 1985 after she became concerned about the repayment of her notes. Bettag told her that the LaRouche organizations stand behind their commitments and that notes were good investments. Bettag explained that money wasn't coming in as fast as they had expected, but that all their loans would be repaid and that her money was safe.

20. After the conversation with Bettag, Mitchell advised

family members about the loans she had made to the Respondents and the delinquencies that existed. Later, with their advice and input, she retained counsel and the Department was eventually informed of the transactions.

21. In later November of 1985, Joyce Rubenstein, a Caucus representative, telephoned Mitchell from New York to discuss her loans to Caucus. Rubenstein advised Mitchell that if she would make an additional $10,000 loan to Caucus she would be sure to get the rest of her money ($40,000) back. Based on these representations, Mitchell loaned Caucus another $10,000 for eight months at 12 percent. On November 29, 1985, Mitchell received confirmation from Caucus that the loan had been made under those terms. Confirmation was in a letter form. No note was issued as had been done in the past.

22. Mitchell considered all of her loans to the Respondents as investments, not unlike certificates of deposit that individuals can purchase from a bank. None of her loans were intended to be contributions and none of them were collateralized. Apart from IDL's note, most of the notes issued were notarized by .Bettag and most specifically stated that they could not be assigned, transferred or discounted. All of them were signed by Fredman.

23. In 1984 and 1985, the Respondents solicited loans from other Minnesota residents and from residents in other states including Illinois, Maryland, Alaska, Indiana, and Washington.

24. No individual employed by or representing the Respondents gave Mitchell any financial information regarding the organizational Respondents that she could use to determine their ability to repay the loans she made. She was not told how the Respondents would be able to repay her loans, where

the money used to repay her loans would come from, or what the risks of her investments were. Mitchell was not advised if Caucus was in default of its obligation to repay principal and interest to other investors or that one judgment had been entered against Caucus for failure to repay a loan when due. : Moreover, Mitchell was never advised that the Respondents were not licensed to sell securities in the State of Minnesota or that the notes were not registered as required by law. In fact, Fredman told Mitchell that the loans were legal.

BASED ON THE FOREGOING FINDINGS OF FACT, THE UNDERSIGNED MAKES THE FOLLOWING:

CONCLUSIONS OF LAW

1. That the Minnesota Commissioner of Commerce and the Administrative Law Judge have authority to consider the issues raised by the Commissioner's Cease and Desist Order and Order Suspending Exemption, as amended, under Minn. Stat. §§ 80A.21, 80A.15, subd. 3, and 14.50 (1984).

2. That the Department has complied with all releyant substantive and procedural requirements of law and rule and that the Respondents received proper and timely notice of the hearing and of the Commissioner's Orders.

3. That under Minn. Rule 1400.7300, subp. 5, the Department has the burden of proof to establish the statutory violations alleged by a preponderance of the evidence.

4. That the loans solicited by Ron Fredman and the notes issued by the organizational Respondents constituted offers and sale for purposes of Minn. Stat. § 80A.14, subd. 17 (1984).

5. That the promissory notes offered and sold by the Respondents in the state of Minnesota constitute securities for purposes of Minn. Stat. § 80A.14, subd. 18 (1984).

6. That the promissory notes offered and sold by the Respondents in the State of Minnesota were not registered with the Commissioner .prior to :or at the time of their offer of sale as required by Minn. Stat. § 80A.08 (1984).

7. That the Respondent Ron Fredman violated Minn. Stat. § 80A.014, subd. 1, by transacting business in this State as an agent without a license to do so.

8. That the organizational Respondents violated Minn. Stat. § 80A.04, subd. 2, by employing Ron Fredman as their agent.

9. That in connection with the sale of promissory notes to Mary Mitchell, the Respondents Ron Fredman and Ronald R. Bettag failed to state material facts necessary in order to make statements that were made not misleading, contrary to Minn. Stat. § 80A.04, clause (b) (1984), by failing to disclose financial information which could have been used to determine the organizational Respondents. ability to repay the notes when due and by failing to advise Mitchell that none of the Respondents were licensed to sell securities in the State of Minnesota and that the promissory notes were not registered pursuant to the Minnesota Securities Act.

10. That the Cease and Desist Order proposed by the Commissioner is in the public interest and should be issued.

11. That under Minn. Stat. § 80A.15, subd. 4, the Respondents have the burden of proving any exemption claimed under Minn. Stat. § 80A.Ol to 80A.31 or any exception from a definition contained therein.

12. That the Respondents have failed to establish that the promissory notes they sold are subject to any exemption or exception.

13. That the Respondent Ron Fredman fraudulently misdated one of the promissory notes issued to Mitchell in violation of Minn. Stat. § 80A.Ol, clause (c) (1984).

14. That the Respondent Ron Fredman did not violate Minn. Stat. § 80A.Ol, clause (c) by telling Mitchell that some banks were failing.

BASED UPON THE FOREGOING CONCLUSIONS OF LAW, THE UNDERSIGNED MAKES THE FOLLOWING:

ORDER

1. That Respondent shall cease and desist from offering or selling any security in Minnesota without filing said security pursuant to Minn. Stat. ch. 80A, or without obtaining an opinion letter from the Department of Commerce that said security is exempt from filing.

2. That Respondents shall cease and desist from offering or selling any promissory notes or other debt instruments without filing said instruments pursuant to Chapter 80A, or without obtaining an opinion letter from the Department of Commerce that the instrument need not be filed.

Dated: Sept. 3, 1987

MICHAEL A..HATCH
Commissioner of Commerce
State of Minnesota
Department of Commerce

500 Metro Square Building
Seventh & Robert Streets
St. Paul, Minnesota 55101

State of Minnesota

In Court of Appeals

C4-87-1952
Department of Commerce
Randall, Judge

CAUCUS DISTRIBUTORS, INC.,
STUART L. FINNEY
ET AL.,
FULLER & FINNEY
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PATRICK J. MORAN
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Relators,

V

COMMISSIONER OF COMMERCE,
HUBERT H. HUMPHREY, III
ATTORNEY GENERAL

JEROME L. GETZ
SPEC. ASST. ATTORNEY GENERAL
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7TH PLACE & MINNESOTA STREET

ST. PAUL, MN 55101
Respondent.

Filed April 5, 1988
Office of Appellate Courts

SYLLABUS

1 A discovery sanction that precluded relators from contesting some of respondent's allegations did not impermissibly deprive relators of an opportunity to be heard. The sanction was for good cause and within the discretion of the Administrative Law Judge (ALJ).

2. The factual findings of the Commissioner were supported by substantial evidence.

3. The promissory notes relators issued constituted securities under Minn. Stat. § 80A.14.

4. The Federal Election Campaign Act does not preempt regulation of the issuance of securities by relator Independent Democrats for LaRouche.

5. Minnesota Security Laws do not impermissibly infringe on relators' first amendment rights to freedom of association.

6. Improper portions of relator's brief and appendix are stricken.

Affirmed.

Heard, considered and decided by Randall, Presiding Judge, Lansing, Judge, and Mulally,* Judge.

OPINION

RANDALL, Judge

This matter is before us on writ for certiorari to review a decision of the Commissioner of Commerce. The Commissioner found promissory notes relators offered and sold in exchange for loans were unlicensed securities. The Commissioner ordered relators to cease offering or selling unfiled promissory notes or debt instruments without obtaining an opinion letter from the department of commerce. This appeal is from the Commissioner's order. We affirm.

FACTS

Relators Caucus Distributors, Inc. (CDI) and Campaigner Publications, Inc. (CPI) are New York corporations. Independent Democrats for LaRouche (IDL) is an unincorporated association.

MM, an 85 year old widow, was the only witness to testify at the hearing. According to MM's testimony, her first contact with respondents was in July 1984. MM was downtown Minneapolis, when she saw an individual passing

* Acting as judge of the Court of Appels by appointment pursuant to Minn. Const. Art. 6,§2.

out pamphlets. MM took a pamphlet and found it discussed Lyndon LaRouche. She heard LaRouche on television a few days earlier, and she told the pamphleteer she liked LaRouche and his views. MM gave the pamphleteer her telephone number so someone could call her and talk about LaRouche.

About a week later, MM received a telephone call from Ron Fredman of the Chicago office. Fredman told MM that the organization could use her help in its efforts to cut down on dope pushing in the Middle East and other places. He also mentioned incidents of banks closing, a matter of which MM was already aware through various newspaper articles.

Fredman asked MM to loan money to the LaRouche organization. MM testified Fredman told her she would get a promissory note, specifying the interest rate and maturity date, and MM said she "thought it was just like something you would give to a bank." In return for a $15,000 three-year loan, MM received two notes, one for $10,000 and another for $5,000.[1] On September 3, 1984, MM made out a check for $1000, payable to IDL. On the bottom of the check, MM made the notation: "1-yr. _____

April 16, 1985, to replace one note for $5000 and one note for $10,000, which had been made out for three years loan at 10%."[2] Shortly after MM mailed the check, she received a note from IDL, signed by Paul Greenberg. Relators stipulate that this was a valid loan, and that Greenberg was authorized to sign the note.

[1] A 12-month, $15,000 note was issued by Caucus Distributors

[2] The loan was paid off, together with interest.

After receiving another telephone call from Fredman, MM made out a check to CDI for $5000. On the bottom of the check, MM wrote: "90-day loan, 15 percent annual rate." MM received a note from CDI in early 1985, after Fredman informed her she could not be repaid within the 90-day period.

About November 26, 1984, MM made another loan to COI for $10,000, "for the same reason that [she] made the other ones. [She] thought it was a good investment * * *." MM received a six-month promissory note dated November 26, 1984, signed by Fredman for CDI in the amount of $10,000, with interest at 16%. Fredman offered her 16% when she told him she had a certificate of deposit (CO) at 14%.

In April 1985, Mr. Fredman called MM and asked to borrow more money from her. MM sent CDI one check for $4000 and another for $6000. She received a $10,000 promissory note at 10% interest from CDI, signed by Fredman. In the fall of 1985, appellant received three checks from CDI, totalling $1000, as partial loan repayment. MM testified she never believed she would not be timely repaid on the notes. She testified she was not informed that CDI was borrowing significant amounts of money from other persons. She did not know that CDI, CPI or IDL had failed to make timely payments on notes issued to other persons. MM did not know that other lenders had not been repaid and had obtained judgments against CDI.

In November 1985, Joyce Rubenstein, from CDI's New York office, telephoned MM, informing her that if she made an additional loan to CDI, the $40,000 total loans would be repaid. When she sent the check to CDI, MM received a letter acknowledging receipt of the loan.

On October 6, 1986, the ALJ issued a discovery order, requiring relators to provide a list of persons who made loans

to relators after September 1, 1983. Relators resisted on the grounds that the names of lenders to LaRouche's campaign were privileged information, and that requirement of their disclosure would somehow interfere with the first amendment right of freedom of association of CDI and its lenders.

The ALJ gave relators an alternative solution. Each relator could provide the ALJ with a comprehensive list of persons who had made loans. The ALJ would provide respondent with thirty names, chosen at random from each list, and respondent could then request additional information about the individuals chosen. The ALJ indicated that the information would be subject to a protective order providing for the confidentiality of the information, and for the return to relators of all information after a final decision was reached.

Relators deliberately did not comply with either option offered by the discovery order, continuing to claim the lists were privileged. Respondents moved for the imposition of sanctions. The ALJ denied the motion, but reaffirmed its prior order and again directed relators to comply with discovery. Relators again informed the ALJ of their decision not to comply with any discovery order. The ALJ then entered an order precluding relators from contesting portions of respondent's amended cease and desist order.

After considering the evidence, and consistent with the ALJ's recommendation, the Commissioner found that relators offered and sold unregistered securities in Minnesota, contrary to the requirement of Minn. Stat. § 80A.08, and ordered relators to cease and desist selling unfiled securities in Minnesota without obtaining an opinion letter from the department of commerce.

ISSUES

1. Did discovery sanctions improperly deprive relators of a right to be heard?

2. Were the factual findings of the Commissioner supported by substantial evidence?

3. Do the promissory notes issued by relators constitute securities under Minn. Stat. § 80A.14?

4. Does IDL constitute a presidential campaign organization, the regulation of which is preempted by the Federal Election Campaign Act?

5. Are relators' fund-raising activities protected by the first amendment?

6. Should materials in relators' brief be stricken?

ANALYSIS

I

DISCOVERY SANCTIONS

Relators contend they had a right to protect their lists of supporters and contributors on first and fourteenth amendment and privacy grounds. They assert that the order requiring disclosure of their membership violated their supporters' rights to free association and speech.

The compelled disclosure of an individual's affiliation with an organization may, standing alone, constitute an intrusion into the first amendment rights of privacy of association and

belief. Jones v. Unknown Agents of the Federal Election Commission, 613 F.2d 864, 874 (D.C. Cir. 1979)(discussing NÅACP v. Alabama, 357 U.S. 449 (1958)).

> [A] court must be particularly mindful of potential damage to associational interests when enforcing a subpoena against minor political parties and their members.

Federal Election Commission v. The LaRouche Campaign, 644 F.Supp. 120, 123 (S.D.N.Y. 1986)(citing Buckley v. Valeo, 424 U.S. 1, 71 (1976)).

However, governmental interests underlying the disclosure provisions of the Federal Election Campaign Act may outweigh the possible harm to the associational rights of members of minor political parties. See NAACP, 357 U.S. at 463.

The state's security laws are aimed at

> speculative schemes having no more basis than so many feet of blue sky, * * * and * * * [they are] intended to put a stop to the sale of shares in visionary oil wells, nonexistent gold mines and other "get-rich-quick" schemes calculated to despoil credulous individuals of their savings. It is a proper and needful exercise of the police power of the state and should not be given a narrow construction * * *. The commission * * * has the power, in making its investigation, to compel a full disclosure of the facts upon which to base an intelligent judgment.

State v. Gopher Tire & Rubber Co., 146 Minn. 52, 55, 177 N.W. 937, 938 (1920). This governmental interest is sufficiently compelling to outweigh the claimed infringement

by relators on their right of association with their contributors.

In LaRouche Campaign, the Federal Election Commission (FEC) sought information to determine whether the LaRouche Campaign had reported false information about contributions and loans. The court concluded that the state's interest was sufficiently compelling to require disclosure of solicitors and contributors. LaRouche Campaign, 644 F.Supp. at 122. The information that could be requested by the FEC included identification of officers, directors and other members insofar as they related to persons responsible for soliciting contributions, and all bank records pertaining to loans and contributions.

Here, the information requested is even less intrusive. The discovery order did not require disclosure of the names of persons soliciting loans, officers, directors, employees and volunteers unless the lists furnished had fewer than 25 names.

Respondents claim they were prejudiced by relators' failure to provide the list. We agree. Relators point out they provided respondent with seven names. However, relators' disclosure of seven names selected by relators did not adequately comply with the order. The ALJ correctly found that relators' failure to provide the required information deprived respondent of the opportunity to prove its case, particularly to prove the instruments were securities. The sanction was appropriate.

II

EVIDENCE TO SUPPORT FINDINGS OF FACT

Decisions of administrative agencies enjoy a presumption of correctness, and deference should be shown by courts to the agency's expertise and special knowledge in its field of

technical training, education, and experience. Reserve Mining Co. v. Herbst, 256 N.W.2d 808, 824 (Minn. 1977). This court must decide whether findings of fact are unsupported by substantial evidence. Id. at 827; Minnesota Administrative Procedure Act, Minn. Stat. § 15.0425 (1984).

Relators claim some of the Commissioner's findings of fact were not supported by the evidence. MM did not testify that Bettag, a consultant for relators, solicited loans from her. Relators claim there was no evidence Bettag had any role in soliciting loans.

However, respondent alleged that Bettag solicited loans. Relators' failure to comply with the ALJ's discovery order deprived respondent of the opportunity to prove this allegation. The ALJ's sanction for failure to comply with discovery precluded relators from contesting, among other things, respondent's claim that Bettag offered or sold promissory notes to persons in Minnesota. Since we affirm the discovery sanctions, we hold the Commissioner's finding was proper.

Relators claim the Commissioner's finding #18 constituted an abuse of discretion:

> During their telephone conversation in 1984 and 1985, [MM] and Fredman primarily talked about Caucus, but he never explained his relationship to Caucus, Campaigner or IOL. In addition, he never told her how they would repay the loans, if they had solicited loans from other persons, or if they had repaid those loans in a timely fashion.

Relators contend that it was unreasonable to assume MM did not realize that other lenders made loans to relators. The contested finding was that relators never told MM how the loans were to be paid, or about other loans or inability to make

other loan payments. That finding is supported by MM's testimony that Fredman never discussed with her how CDI would repay the loans, that COI was borrowing significant amounts of money from other persons, or that CDI had failed to make timely repayment on notes CDI had issued to other persons. She testified no one connected with CPI, IDL or CDI told her that any of those organizations had failed to make timely payments on loans to other persons.

Relators contend there was inadequate evidence to support finding #22, that MM "considered all of her loans to [relators] as investments, not unlike certificates of deposit * * *." When asked why she made a particular loan to CDI, MM testified: "[F]or the same reason that I made the other ones. I thought it was a good investment on there." MM testified Fredman offered her a note at 16% when she told him she had money invested in a CO at 14%. MM testified that she has quite a few CD's, and thought of them and bank accounts as investments. MM testified

> as long as he told me I could give a promissory note and specify the interest and when I would get repaid, I thought it was just like something you would give to a bank. * * * I said, "Well, if it's just a loan for a year or so, I could put it in the bank anyhow, so he could have it."

MM's testimony supports the finding.

III

SECURITIES

The Commissioner found that "the promissory notes offered and sold by [relators] in the State of Minnesota constitute securities for purposes of Minn. Stat. § 80A.14,

subd. 18 (1984)." The statute includes in its definition of "security:"

> any note; stock; treasury stock; bond; debenture; evidence of indebtedness; certificate of interest * * *.

Id. In a judicial or administrative proceeding under Minn. Stat. §§ 80A.01-.31, the burden of proving an exemption or an exception from a definition is upon the person claiming the exemption or exception. Minn. Stat. § 80A.15, subd. 4 (1984).

Both parties agree there is no applicable Minnesota caselaw defining security in a context similar to the notes at issue here. However, they agree that appropriate analysis would be under federal law interpreting the Securities Act of 1933, 15 U.S.C. §§ 77a-77bbbb, and the Securities Exchange Act of 1934, 15 U.S.C. §§ 78a-78kk.

Relators point out that the term "security" has the meaning given to it in the statute unless the context requires otherwise. Minn. Stat. § 80A.14, subd. 1 (1984). Relators contend that viewed in the context of the transaction, its notes are not securities within the definition of Minn. Stat. § 80A.14. Respondent agrees that it would be inappropriate to consider all notes securities, but claims the Commissioner properly found the notes at issue here to be securities.

Under a literal application of Minn. Stat. 80A.14, subd. 18, which specifically refers to notes as securities, the promissory notes would be securities. In Landreth Timber Co. v. Landreth, _ U.S. _, 105 S.Ct. 2297 (1985), the Supreme Court found instruments bearing the name and the usual characteristics of stock had to be treated as a security under the plain meaning of the statutory definition.

A literal interpretation is, however, inappropriate for the

term "note," which

> may now be viewed as a relatively broad term that encompasses instruments with widely varying characteristics, depending on whether issued in a consumer context, as commercial paper, or in some other investment context.

Id. at __, 105 S.Ct. at 2306.

Some courts have applied an investment contract analysis to determine whether a document is a security. In Securities & Exchange Commission v. W.J. Howey Co., 328 U.S. 293 (1946), the Supreme Court defined an investment contract, a security under the federal act, as:

> a contract, transaction or scheme whereby a person invests his money in a common enterprise and is led to expect profits solely from the efforts of the promoter or a third party, it being immaterial whether the shares in the enterprise are evidenced by formal certificates or by nominal interests in the physical assets employed by the enterprise.

Id. at 298-99. See also Gopher Tire, 146 Minn. at 56, 177 N.W. at 938 ("investment contract" found to mean contract or scheme for "placing of capital or laying out of money in a way intended to secure income or profit from its employment").

The Howey test has been applied to documents similar to the notes issued by relators. See Securities & Exchange Commission v. World Radio Mission, Inc., 544 F.2d 535 (1st Cir. 1976). World Radio Mission was a religious organization which raised funds by selling interest-bearing notes. The court found the documents were securities, both within the plain meaning of the statute and under the investment contract analysis, as applied in United Housing Foundation, Inc. v. Forman, 421 U.S. 837 (1975). Id. at 852. Several federal

courts have rejected the Howey test, however. See Daily v. Morgan, 701 F.2d 496 (5th Cir. 1983); Exchange National Bank of Chicago v. Touche Ross & Co., 544 F.2d 1126 (2d Cir. 1976).

Relators contend the courts must look for the characteristics of an investment, i.e. "the expectation of profit based upon the entrepreneurial or managerial efforts of others." See Great Western Bank & Trust v. Kotz, 532 F.2d 1252 (9th Cir. 1976).

> To determine whether the transaction under review involves an "investment" in return for "securities" within the meaning of the securities laws, we analyze the nature and degree of risk accompanying the transaction to the party providing the funds. * * * The inquiry is whether the funding party invested "risk capital."

Id. at 1256-57 (citations omitted). The Kotz court found the ultimate inquiry to be whether the lender, a bank that received an unsecured note in exchange for a loan, contributed "risk capital" subject to the entrepreneurial or managerial efforts of the issuer of the note. Id. at 1257.

Relators argue MM made the loans with only an expectation of a set rate of interest not contingent upon the managerial or entrepreneurial efforts of relators, and therefore the loans are not securities. See Union Planters National Bank of Memphis v. Commercial Credit Business Loans, Inc., 651 F.2d 1174, 1185 (6th Cir. 1981)(loan participation purchased by bank did not constitute security, where bank considered transaction a loan, not an investment, the existence of collateral strongly suggested a commercial loan, and the interest payments were to be made from the efforts of a third party).

Here, the notes are securities under the Kotz test. MM's loans to relators were not collateralized; the loans made to MM

and to other individuals were not isolated transactions, but part of a general offering; and the notes were not short-term demand notes. This case can be distinguished from Union Planters, in that the ability to repay the loan and interest was directly dependent on the fund-raising efforts of relators, and not upon the managerial or entrepreneurial efforts of some third party.

Among the factors to consider when determining whether the notes were purchased as an investment or as a commercial loan are whether the notes were personal promissory notes issued by a private party; whether the notes were offered to the public; whether the issuer is the person bringing the claim; and whether the notes were procured in the solicitation of venture capital. See Lino v. City Investing Co., 487 F.2d 689, 694-95 (3d Cir. 1973).

Relators contend that MM did not make an investment because she expected to get back only her principal plus interest, and did not expect to share in any profits of enterprises conducted by relators. MM risked the loss of her capital in return for loans at an interest rate up to two percentage points above the rate she was receiving on her CD.

The following factors weigh in favor of finding the notes are securities under the commercial/investment dichotomy test:

1 MM is not a financial institution or commercial lender in the business of making loans to private parties;

2 The notes Were not issued in connection with consumer installment transaction or real estate purchase;

3 The notes were not collateralized;

4 The sale took place outside the normal market for notes and commercial paper;

5 The sales to MM took place as part of a broader solicitation of loans from members of the public;

6 MM considered the notes an investment;[3]

7 The notes are securities within the plain meaning of the statute .....

Relators point out that MM thought of the notes like certificates of deposit. Certificates of deposit issued by federally regulated banks are not securities. Marine Bank v. Weaver, 455 U.S. 551, 559 (1982). However, relators ignore the Supreme Court's reasoning:

> It is unnecessary to subject issuers of bank certificates of deposit to liability under the antifraud provisions of the federal securities laws since the holders of bank certificates of deposit are abundantly protected under the federal banking laws.

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[3] She was unwilling to make contributions in excess of $25 to appellants, but was prevailed upon to make substantial loans ($40,000), by promises of higher interest, including at one point interest two percentage points higher than interest she was currently receiving on a CD.

Id. The certificate of deposit analogy is not applicable here. MM and other lenders do not benefit from the protection of federal or state banking laws. An important consideration is that the purpose of the securities law is to protect members of the public from fraud and imposition. Gopher Tire, 146 Minn. at 55, 177 N.W. 938; see also State v. Investors Security Corp., 297 Minn. 1, 8, 209 N.W.2d 405, 409 (1973)(in accordance with an expansive view of our securities statutes, there has been a consistent broadening of the coverage of these statutes in Minnesota). We find, unequivocally, that this policy is furthered by our holding here that the Commissioner correctly found these notes to be securities under Minn. Stat. §80A.14 (1984) and subject to regulation by the State of Minnesota.

IV

FEDERAL PREEMPTION

Relators point out that state law may be preempted where congress enacts federal statutes with the clear intent of preempting state law. See Silkwood v. Kerr-McGee Corp., 464 U.S. 238, 248 (1984). Generally, a federal act does not supersede the police power of the state unless that was the clear and manifest purpose of Congress. Jones v. Rath Packing Co., 430 U.S. 519, 525 (1977)(quoting Rice v. Santa Fe Elevator Corp., 331 U.S. 218, 230 (1947)). The federal-state balance will not be disturbed unintentionally by Congress or unnecessarily by the courts. See id. The test is whether, in the relationship between state and federal law as applied, the state law "stands as an obstacle to the accomplishment and execution of the full purposes and objectives of Congress." Hines v. Davidowitz, 312 U.S. 52, 67 (1941).

Respondent argues that Congress did not intend to preempt laws of general application outside the area of election, that

there is no conflict between the federal election laws and state law, and that compliance with one does not preclude compliance with the other. We agree that Minnesota security laws, as applied here to protect Minnesota residents, do not conflict with the intent of the federal election laws.

Relators would have this court hold that the federal laws relating to elections and political activities supersede and preempt any state law provision with respect to federal office, giving appellants absolute immunity from state law simply because LaRouche has aspirations to federal office. We decline to do so.

V

FIRST AMENDMENT ARGUMENTS

Relators argue that because they are political organizations, the first amendment protects them from application of state regulation. See generally Federal Election Commission v. Massachusetts Citizens for Life, Inc., _ U.S. _, 107 S.Ct. 616 (1986)(federal statute restricting independent spending unconstitutionally infringed on free speech without compelling justification). However, the bare claim of a first amendment interest does not insulate behavior from responsible judicial scrutiny. The state has an interest in protecting citizens from abusive practices in solicitation of funds for charity, even when the charitable Organization has a purpose protected by the first amendment. See Cantwell v. Connecticut, 310 U.S. 296, 306 (1940).

In World Radio Mission, notes made in exchange for loans to a religious organization were found to be securities. World Radio Mission asserted first amendment freedom of religion rights. The First Circuit Court of Appeals found that World Radio did not solicit contributions, but stressed the security of

investment. World Radio Mission, 544 F.2d at 538-39. The court pointed out the 12% interest rate "suggests defendants' investors were moved by something more than a donative spirit." Id. at 539. Having solicited funds on economic grounds, the court found, World Radio could not claim first amendment protection. MM, by her own uncontradicted testimony, stated she was induced, not by LaRouche's oratory or his political platform, but by high interest rates, to lend the money.

Similarly, relators here were not engaging in an activity protected by the first amendment when they issued promissory notes in exchange for loans. As in World Radio Mission, MM was motivated by "something more than a donative spirit." MM's testimony supports the Commissioner's finding that MM considered the loans investments and did not intend to make contributions. As purveyors of these "investments," relators cannot claim first amendment protection shields them from reasonable state regulation and reasonable scrutiny by the courts.

VI

STRIKING OF APPENDIX

Respondent requests this court to strike from the appendix a copy of a loan repayment agreement of the Ronald Reagan Congressional Victory Fund. Appellant claims this is the sort of thing to which MM referred when she said

> money is lent to Democrats, Republicans right along, and then they pay it when they get it. Where they get it from or how they arrange it, I don't know about it.

The record is devoid of evidence that MM had ever seen the victory fund document, and thus no evidence exists that she either relied on it or compared the notes in question to that

"loan repayment agreement." Additionally, the document was not introduced at trial. Portions of an appendix that were not before the trial court are not properly before this court. See State v. Edmison, 373 N.W.2d 639, 640 (Minn. Ct. App. 1985), reviewed and remanded on other grounds, 379 N.W.2d 85 (Minn. 1985).

Respondent objects to other portions of relators' brief containing information not in evidence. For instance, relators' brief refers to fund-raising activities of Republicans. Relators argue that such activities were overlooked, and that they are the victims of selective enforcement against minority political groups. The record does not support this accusation; this issue was not briefed, raised and argued to the ALJ, and will not considered on appeal.

Respondent also challenges a statement in relator's brief alleging some states received lists of lenders from Virginia or the federal authorities, and that it was probable Minnesota also received a list of Minnesota residents who ere lenders. Relators inferred from this claim that the discovery order they resisted was therefore unnecessary. Relators admit that this information was not in evidence, but assert it is common knowledge, and assert it is common knowledge, and assert these statements were never refuted. The statement that Minnesota "may have" received such a list is, by its phrasing, speculative, and , without more, we do not consider it. We grant respondent's motion to strike portions of relators' appendix. We note that our decision to strike these relatively immaterial portions has no bearing on our disposition of the issues in this case.

DECISI0N

The ALJ's discovery sanctions did not impermissibly deprive relators of the opportunity to present issues and argue

their case. The factual findings of the ALJ are supported by substantial evidence. The promissory notes relators issued constitute securities under Minn. Stat. §80A.14. The Federal Election Campaign Act does not preempt regulation of the issuance of securities by relator Independent Democrats for LaRouche. Minnesota security laws, as applied to relators fund raising activities, do not impermissibly infringe on relator's first amendment right of association. Portions of relators' brief and appendix are stricken.

Affirmed.

Blue Sky Law

(3) the security registered or sought to be registered is the subject of an administrative stop order or similar order or a permanent or temporary injunction of any court of competent jurisdiction entered under any other federal or state act applicable to the offering; but (i) the commissioner may not institute a proceeding against an effective registration statement under this clause more than one year from the date of the order or injunction relied on, and (ii) may not enter an order under this clause on the basis of an order or injunction entered under any other state act unless that order or injunction was based on facts which would currently constitute a ground for a stop order under this section;

(4) the issuer's enterprise or method of business includes or would include activities which are illegal where performed;

(5) the offering has worked or tended to work a fraud upon purchasers or would so operate;

(6) except with respect to securities which are being registered by notification, the terms of the securities are unfair and inequitable; provided, however, that the commissioner may not determine that an offering is unfair and inequitable solely on the grounds that the securities are to be sold at an excessive price where the offering price has been determined by arms length negotiation between nonaffiliated parties. The selling price of any security being sold by a broker-dealer licensed in this state shall be presumed to have been determined by arms length negotiation;

(7) when a security is sought to be registered by coordination there has been a failure to comply with the undertaking required by section 80A.10, subdivision 2, clause (d);

(8) the applicant or registrant has failed to pay the proper filing fee; but the commissioner may enter only a denial order under this clause and he shall vacate any such order when the deficiency has been corrected; or

(9) the offering of securities sought to be registered is not firmly underwritten and (i) the minimum amount of proceeds from the sale of the securities is not more than $500,000, and (ii) the maximum amount of proceeds is more than 200 percent of the minimum amount of proceeds required to go forward with the offering.

The commissioner may not institute a stop order proceeding against an effective registration statement solely on the basis of a fact or transaction known to him when the registration statement became effective unless the proceeding is instituted within the next 30 days.

Subd. 2. The commissioner may issue an order requiring the person for whom a registration was made to show cause why the registration should not be revoked. The order shall not b calculated to give reasonable notice of the time and place for hearing thereon, and shall state the reasons for the issuance of the order. The commissioner may by order summarily suspend a registration pending final determination of an order to show cause. a hearing on the merits shall be held within 30 days of the issuance of the order or suspension. All hearings shall be conducted in accordance with the provisions of chapter 14 [Administrative Procedure]. After the hearing, the

commissioner shall enter an order making such disposition of the matter as the facts require. If the person for whom the registration was made fails to appear at a hearing of which he has been duly notified, such person shall be deemed in default and the proceeding may be determined against the person upon consideration of the order to show cause, the allegations of which may be deemed to be true. The commissioner may adopt rules of procedure concerning all proceedings conducted pursuant to this subdivision.

[¶33,114]

Sec.80A14.Definitions. Subdivision 1. *Terms*. When used in sections 80A.01 to 80A.31, the terms defined in this section have the meanings given them unless the context otherwise requires.

Subd.2 *Affiliate*. "Affiliate" of another person means any person directly or indirectly controlling, controlled by, or under common control with the other person.

Subd. 3 *Agent*. "Agent" means any individual other than a broker-dealer who represents a broker-dealer or issuer in effecting or attempting to effect purchases or sales or securities. "Agent" does not include an individual who represents an issuer in:

(1) effecting transactions in a security exempted by section 80A.15, subdivision 1;

(2) effecting transactions exempted by section 80A.15, subdivision 2;

(3) effecting transactions with existing employees, partners or directors of the issuer if no commission or other...

subdivision of a government or any other entity.

Subd. 16 *Purchasing for investment.* "Purchasing for investment" means a purchase made for investment and not for the purpose of resale. In determining whether securities have been purchased for investment, the length of the period for which the securities are held will be one of the factors considered. Securities held fr two years after their purchase shall be conclusively deemed to have been purchased for investment.

Subd. 17. *Sale, sell.* (1) "Sale" or "sell" includes every contract of sale of , contract to sell, or disposition of , a security or interest in a security for value.

(2)"Offer" or "offer to sell" includes every attempt or offer to dispose of, or solicitation of an offer to buy, a security or interest in a security for value.

(3) Any security given or delivered with, or as a bonus on account of, any purchase of securities or any other thing is considered to constitute part of the subject of the purchase and to have bee offered and sold for value.

(4) A purported gift of assessable stock is considered to involve an offer and sale.

(5) Every sale or offer of a warrant or right to purchase or subscribe to another security of the same or another issuer, as well as every sale or offer of a security which gives the holder a present or future right or privilege to convert into another security of the same or another issuer, is considered to include an offer of the other security.

(6) The terms defined in this subdivision do not include (i) any bona fide pledge or loans; (ii) any stock dividend, whether the corporation distributing the dividend is the issuer of the stock or not.

Subd. 18. *Security*. (a) "Security" means any note; stock; treasury stock; bond; debenture; evidence of indebtedness; certificate of interest or participation in any profit sharing agreement; collateral trust certificate; preorganization certificate or subscription; transferable shares; investment contract; investment metal contract or investment gem contract; voting trust certificate; certificate of deposit for a security; certificate of interest or participation in an oil gas or mining right, title or lease or in payments out of production under the right, title or lease; or, in general, any interest or instrument commonly known as a security, or any certificate of interest or participation in, temporary or interim certificate for, receipt for guarantee of , or warrant or right to subscribe to or purchase, any of the foregoing. "Security" does not include:

(1) any insurance or endowment policy or annuity contract under which an insurance company promises to pay money either in a lump sum or periodically for life or for some other specified period; or

(2) stock of a closely-held corporation offered or sold pursuant to a transaction in which 100 percent of the stock of that corporation is sold as a means to effect the sale of the business of the corporation if the transaction has been negotiated on behalf of all purchasers, and if all purchasers have access to inside information regarding the corporation before consummating the transaction.

(b) A security that is offered and sold pursuant to section 4(5) of the Securities Act of 1933 or that is a "mortgage related security" (as defined in section 3(a)(41) of the Securities

Exchange act of 1934) is not a security exempt from registration under section 80A.15, subdivision 1 paragraph (a), in the same manner as obligations issued or guaranteed as to principal and interest by the United States or its agencies or instrumentalities. This provision specifically overrides the preemption of state law contained in section 106(c) of the Secondary Mortgage Market Enhancement Act of 1984, Public Law Number 98-440.

Subd.19. *State.* "State" means any state, territory or possession of the United States, the District of Columbia and Puerto Rico.
[Sec.80A.14 amended by Laws 1986, Ch. 358,Laws 1987, Ch.336.]

[¶33,115]

Sec.80A.15 Exemptions. Subdivision 1. The following securities are exempted from sections 80A.08 and 80A.16:

(a) Any security, including a revenue obligation, guaranteed by the United States, any state, any political subdivision of a state or any corporate or other instrumentality of one or more of the foregoing; but this exemption shall not include any industrial revenue bond. Pursuant to section 106(c) of the Secondary Mortgage Market Enhancement Act of 1984, Public Law Number 98-440, this exemption does not apply to security that is offered or sold pursuant to section 106(a)(1) or (2) of that act.

(b) Any security issued or guaranteed by Canada, any Canadian province, any political subdivision of any province, any agency or corporate or other instrumentality of one or more of the

STATE OF MINNESOTA

IN THE SUPREME COURT
CAUCUS DISTRIBUTORS, INC., ET AL
Petitioners

V.

COMMISSIONER OF COMMERCE
Respondent

PETITION FOR REVIEW
OF DECISION OF COURT
OF APPEALS
Appellate Court Case

DATE OF FILING OF COURT OF APPEALS
DECECISION: April 5, 1988

No. C4-87-1952

TO: The Supreme Court of the State of Minnesota

The Petitioners, Caucus Distributors, Inc., Campaigner Publications, Inc., and Independent Democrats for LaRouche request a Supreme Court review of the above entitled decision of the Court of Appeals upon the following grounds:

I. STATEMENT OF FACTS AND PROCEDURAL HISTORY

Petitioners are New York corporations. Independent Democrats for LaRouche is an unincorporated association organized and qualified under the Federal Election Campaign Act, 88 Stat. 1263. Martha Mitchell, a Minnesota citizen, approached by an individual passing out informational pamphlets took one and purchased a subscription to some publications supporting viewpoints also supported by Lyndon R. LaRouche. She had previously heard Mr. LaRouche on television and was in sympathy with his views.

Subsequently, Martha Mitchell made several loans to Petitioners, some of which were repaid, some of which were not. The only loan made to Independent Democrats for LaRouche in the amount of $1,000.00 was in conformity with the specific regulations of the Federal Election Commission. It was duly repaid. In return for the loans, Petitioners gave notes specifying the amount of the loan and interest rates. The notes ranged for various periods of time from three months to three years.

Minnesota issued a Cease & Desist Order on July, 1986 and a hearing was held August 4, 1986; on October 6, 1986 the administrative law judge issued a discovery order requiring Petitioners to provide a list of persons who made loans to Petitioners after September 1, 1983. Petitioners resisted on the grounds that the release of the names of their lenders would have a chilling effect on the exercise of the first amendment rights of those lenders. Almost half of the lenders requested their names not be disclosed to the Attorney General. The Administrative Law Judge ruled a prima facie chilling effect showing had been made. The administrative law judge then imposed sanctions precluding Petitioners from

contesting portions of the amended cease and desist order, effectively defaulting Petitioners.

On September 3, 1987, Michael A. Hatch, Commissioner of Commerce, found that Petitioners had offered and sold unregistered securities in the State of Minnesota and ordered Petitioners to cease and desist.

II. STATEMENT OF LEGAL ISSUES AND THEIR RESOLUTION BY THE COURT OF APPEALS

Petitioners appealed to the Minnesota Court of Appeals and the decision of the Court of Appeals was filed April 5, 1988.

The Minnesota Court of Appeals found that:

(1) Discovery sanctions did not impermissibly deprive Petitioners of a right to be heard;

(2) The factual findings of the Commissioner were supported by
substantial evidence;

(3) The promissory notes evidencing loans to Petitioners were securities under Minnesota Statute Section 80A.14;

(4) The Federal Election Campaign Act does not preempt regulation of securities in reference to Independent Democrats for LaRouche:

(5) Minnesota securities laws as applied in this matter did not impermissibly infringe on Petitioner's first amendment rights of association, and;

(6) Certain materials were stricken from Petitioner's brief.

Specifically, a copy of a loan repayment agreement of the Ronald Reagan Congressional Victory Fund and other portions of Petitioner's brief referring to fund raising activities of Republicans.

Sanctions imposed by the administrative law judge in this matter for Petitioner's resistance to the State's discovery orders, were improper and, in fact, resulted in Petitioners being unable to present their case. Those discovery requests were for Petitioner's contributor and lender list. Were Petitioner's contributors and lenders to believe their names would become a matter of public record and be circulated among state departments who happened to be politically opposed to them, this would have a chilling effect on those contributors and lenders willingness to support Petitioner's organizations. See Britt v. Superior Court of San Diego County, 574 P.2d 766 (1978) and FEC v. Hall Tyner Election Campaign Committee, 678 F.2d 416 (1982). The State had sufficient facts available through testimony of parties to the transaction and through their own investigation to determine whether or not the loan in question was a security. See also Savika v. Webster. 644 F.2d 743 (1981).

The second issue is that the Commissioner made certain factual findings that were not supported by the record. There was no evidence in the record to suggest that Mr. Bettag solicited loans. The testimony of Mrs. Mitchell was that she only spoke with Mr. Bettag about payments (Tr. 85) and these were already after she had made the loans. (Tr. 98) Mrs. Mitchell testified that the only one who asked her to make loans was Appellant Fredman. (Tr. 98-99) The Court of Appeals made a finding that Bettag sold loans based on the assumption that the evidence which was not produced in response to the discovery request would have shown this. This was patently false, as Mrs. Mitchell did testify that Bettag solicited no loans.

The third issue is the Gravamen of this case since if the notes in question were not securities, then the State's intrusion into the activities of Petitioners would have been improper. The notes in question are not securities and that the Minnesota Act itself coupled with applicable case law indicates that the term security only has the meaning given to it that the context involved requires. See Landreth Timber Company v. Ivan K. Landreth, 471 U.S. 681, 105 S.Ct 2297, 85 L.Ed.2d 692 (1985); Lino v. City Investing Company, 487 F.2d 689 (3rd Cir., 1973). The transaction in question in this case did not bear the characteristics of an investment. There was no "expectation of profit based upon the entrepreneurial/managerial skill of others." Great Western Bank X Trust v. Kotz, 532 F.2d 1252 (9th Cir., 1976). Further, these loans were made with only the expectation of a set rate of interest not contingent upon the managerial or entrepreneurial efforts of Petitioners. Therefore, the loans are not securities. Union Planters National Bank of Memphis v. Commercial Credit Business Loans, Inc., 651 F.2d 1174, 1185 (6th Cir., 1981). The Court of Appeals in this matter essentially found that these notes in question were securities because the Minnesota Act must be construed as broadly as possible in order to protect members of the public.

Petitioners contend that the application of the Minnesota Securities Law to the Independent Democrats for LaRouche organization raises a federal preemption issue since the Federal Election Campaign Act expressed Congress' intent to preempt this area. See Silkwood v. Kerr-McGee Corp., 104 S.Ct 615, 621 (1984). Specifically, Petitioners contend that Section 301 of the FEC Act Amendments of 1974 at 2 U.S.C. Section 453 provide:

> "The provision of this Act and the rules prescribed under this Act supersede and preempt any provision of state law with

respect to election of federal office."

Finally, Petitioners argue that because they are a political organization, the First Amendment protects them from a broad and forced disclosure of information in connection with their first amendment activities. The First Amendment would require that the definition of security be made much less broad due to the first amendment impact on the context of the transactions involved. There is and should be a distinction between a transaction for political purposes and one for commercial purposes. See in re Primus, 436 U.S. 412 (1978) and Ohralik v. Ohio State Bar Association, 436 U.S. 447 (1978).

For these reasons, the Petitioner seeks an order granting review of the decision of the Court of Appeals.

DATED:

Respectfully submitted,

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COM/S-86-047-JL

8-1005-698-2

STATE OF MINNESOTA
OFFICE OF ADMINISTRATIVE HEARINGS

FOR THE MINNESOTA DEPARTMENT OF COMMERCE

In the Matter of Caucus Distributors, Inc., and Campaigner Publications, Inc., New York Corporations,Independent Democrats For LaRouche,an Unincorporated Association, RonFredman, Ronald R. Bettag, Paul Greenberg, and All Other Persons and Organizations Acting in Concert with the Named Respondents.

The above-entitled matter came in for hearing before Administrative Law Judge Jon L. Lunde commencing at 9:00 a.m. on Monday, August 4. 1986 at the Office of Administrative hearings in Minneapolis, Minnesota. Additional proceedings were held the following day. The hearings were held pursuant to a Cease and Desist Order, Notice of Right to Hearing and Order Suspending Exemption issued by the Commissioner of Commerce on June 4, 1986. and an Amended Cease and Desist Order. Notice of Right to Hearing and Order Suspending Exemption issued by the Deputy Commissioner of Commerce on July 17, 1986.

Jerome L. Getz, Special Assistant Attorney General, 1100

Bremer, Seventh Place and Minnesota Street. St. Paul, Minnesota 55101. appeared on behalf of the Minnesota Department of Commerce (Department). Patrick J. Moran, Moran & Pilger, P.A.. Attorneys at Law. 1221 Lamar, Suite 517, Houston, Texas 77010, appeared on behalf of each of the above-captioned organizations and individuals. The record closed on May 20. 1987, when the last authorized brief was filed.

This Report is a recommendation, not a final decision. The Commissioner of the Minnesota Department of Commerce will make the final decision after a review of the record which may adopt, reject or modify the Findings of Fact, Conclusions, and Recommendations contained herein. Pursuant to Minn. Stat. § 14.61, the final decision of the Commissioner shall not be made until this Report has been made available to the parties to the proceeding for at least ten days. An opportunity must be afforded to each party adversely affected by this Report to file exceptions and present argument to the Commissioner. Parties should contact Michael A. Hatch, Commissioner of Commerce. State of Minnesota, Fifth Floor Metro Square Building, St. Paul. Minnesota 55101 to ascertain the procedure for filing exceptions or presenting argument.

STATEMENT OF ISSUES

The issues in this proceeding, as set forth in the Amended Cease and Desist Order of July 17. 1986, are as follows:

> Whether the Respondents offered and sold unregistered securities consisting of promissory notes to Minnesota residents and did so without the requisite licenses.

Whether all or any one of the Respondents fraudulently misdated a promissory note issued 10 a Minnesota resident and fraudulently or deceitfully advised the prospective purchaser of promissory notes issued by the Respondents that some banks were failing, contrary to the provisions of Minn. Stat. § 80A.Ol(c).

Whether the Respondents or any of them failed to state material facts necessary to make statements made during the offer and sale of promissory notes not misleading in violation of Minn. Stat. § 80A.Ol. clauses (b) and (c).

Based upon all of the proceedings herein, the Administrative Law Judge makes the following:

FINDINGS OF FACT

1. Caucus Distributors, Inc. (Caucus' is a Not-For-Profit corporation incorporated under the laws of the State of New York. The Certificate of Incorporation its incorporators filed with the New York Department of State on April 5, 1982 reads in part as follows:

2. The corporation * * * is not formed for pecuniary profit or financial gain, [and] * * * no part of the assets, income or profit of the corporation is distributable to, or inures to the benefit of its members, directors or officers or any private person except to the extent permissible under the Not-For-Profit Corporation Law.

3. The purposes for which the corporation is formed are:

> To promote and encourage the political.and [sic] ideas and beliefs fostered by the International Caucus of Labor Committees and other organizations advocating the same ideas and beliefs; to distribute to the general public, sell and obtain subscriptions to publications specifically dedicated to the political ideas and beliefs fostered by the International Caucus of Labor Committees and other organizations to sclicit membership for certain membership organizations associated with the publications distributed by the corporation consonant with the goals, purposes and programs of those organizations;
>
> to advertise and promote the publications distributed by the corporation;
>
> to engage the services of writers, reporters, editors, distributors. corporations, associations, partnerships and news agencies in furtherance of these purposes;
>
> * * *

2. Campaigner Publications, Inc. (Campaigner) is a New York corporation.

3. Independent Democrats for LaRoiche (IDL) is an unincorporated association and a political committee apparently recognized by the Federal Election Commission. Paul Greenberg is an authorized representative of IDL and is empowered to sign notes on its behalf.

4. At all times material to this case. Ron Fredman and Ronald R. Bettag worked for Caucus and solicited loans to Caucus, IDL and Campaigner by selling notes for them.

5. Ron Fredman. Ronald R. Bettag and Paul Greenberg are not and have never been licensed by the Department to sell securities in the State of Minnesota. Likewise, Caucus, Campaigner and IDL are not and never have been licensed by the Department to sell securities in the State of Minnesota.

6. Mary M. Mitchell, an 85-year-old widow. is a resident of Minneapolis. Minnesota. She has lived there since moving from Winona in 1938. Mitchell is a retired stenographer who has a high school education.

7. In July, 1984, while walking on the Mall near Seventh and Nicollet in downtown Minneapolis. Mitchell was given a pamphlet pertaining to the presidential candidacy of Lyndon LaRouche. She told the man who gave her the pamphlet that she had seen LaRouche on television and liked what she saw. The man told her that if she gave him her name and telephone number someone would call her with more information about LaRouche. She gave him that information.

8. Approximately one week after her encounter on the Mall. Ron Fredman telephoned Mitchell from Chicago to talk to her about LaRouche, Caucus. Campaigner and IDL. Fredman told Mitchell about corruption in the world and the need for Americans to clean it up. He specifically mentioned drug trafficking in the Middle East and South America. the laundering of Mafia money by banks, the decline in American culture, and bank failures. He told Mitchell that some banks were shaky and that if the United States didn't pull together, everyone would go bankrupt. Fredman told Mitchell that LaRouche needed her help with these problems and he asked her for a contribution. She agreed to make a $25 contribution

at that time, and he made arrangements for her to receive copies of "New Solidarity" and other publications.

9. During that initial telephone conversation, Fredman also asked Mitchell to help by making loans. Fredman told her that she would receive a promissory note for any loans she made and that she could specify the interest rate and the term of the notes. Since she would get a promissory note and could specify the interest rate, Mitchell concluded that the loans would be similar to a banking transaction. Moreover, since LaRouche was "in the limelight", she concluded that she was not dealing with a fly-by-night operation that would skip the country, and that her loans would be a good investment. Therefore, she agreed to make a $15,000 loan at that time. In return, she was to receive two notes payable at the end of three years. One was to be made payable to her and her stepson, R. Keith Mitchell, in the principal amount of $10,000. The other was to be.made payable to her and her sister-in-law, Mozell Hall, in the principal amount of $5,000. Fredman personally collected two checks in the aggregate amount of $15,000 from Mitchell at her home in Minneapolis early in July 1984. Later that month. two promissory notes were mailed to her in the aggregate principal sum of $15.000. The notes stated the payees, amounts, term and interest rate Fredman promised.

10. On September 3, 1984, Fredman called Mitchell again and asked her to loan $1.000 to IDL. She agreed to make a $1,000 loan to IDL for one year at ten percent interest. Following her conversation with Fredman. she mailed him a $1.000 check payable to IDL's order. A few days later, she received a promissory note signed by Paul Greenberg, as an authorized representative of IDL. The note was in the principal sum of $1,000. bore interest at the rate cf ten percent, and was payable in one year. The note, and accumulated interest thereon, was paid by IDL in July 1986.

11. On or about September 17, 1984, Fredman telephoned Mitchell again to give her an update on the activities of the LaRouche organizations. At that time, he gave her more information on their efforts to eliminate drug traffic and related activities in the Middle East. In addition, he talked about a publication entitled "Dope. Incorporated" which one of the organizational Respondents had published. During that telephone conversation, Mitchell agreed to make an additional $5.000 loan to Caucus for 90 days with interest at 15 percent. Immediately after her telephone conversation with Fredman, Mitchell mailed him a check payable to Caucus in that amount. A few days later, Mitchell received Caucus' promissory note incorporating the loan terms she and Fredman had discussed.

12. On or about November 26, 1984. Fredman called Mitchell to solicit another loan. During that conversation, Mitchell expressed regret for having made the initial $15,000 loan for a term of three years. He told her that if she returned the notes to him, he would issue two new notes which would mature in a year (on November 26, 1985). At that time, Fredman persuaded Mitchell to make an additional $10,000 loan to Caucus for six months. When Mitchell told Fredman she was getting 14 percent on a certificate of deposit with her bank, he said that Caucus would pay 16 percent on the loan.

13. On or about November 26, 1984, a $10,000 promissory note signed by Fredman for Caucus was mailed 10 Mitchell. It reflected a six-month term and a 16 percent interest rate as she and Fredman had agreed on November 26. At the same time, Mitchell was mailed two promissory notes replacing those which she had returned due to her dissatisfaction with their three-year maturity date. Exhibits 19 and 23. Those notes were signed by Fredman for Campaigner

and reflected a one-year term and a 12 percent interest rate. The payees were the same as those in the notes originally issued.

14. Caucus' September 17, 1984 note for $5,000 was due on December 17, 1984. On or about the due date, Fredman called Mitchell and told her that the note could not be paid because their assets had been frozen by a bank, and he asked her if she would accept a one-third partial payment. Although Mitchell agreed that the bank's explanation for freezing Caucus' funds was "outlandish", she said she would like half of the note paid. Fredman said he would see if that could be done and call her back. Early in January, 1985, after Mitchell returned from a vacation, Fredman called her and asked if she would accept a new note covering Caucus' $5,000 loan to be payable in five monthly principal installments of $1,000 commencing May 1, 1985 and a lump sum interest payment on October 1, 19B5. She agreed and a short time later received a new promissory note from Caucus in the principal sum of $5,000.

Exhibit 17. That note contained the payment terms she had agreed to accept and was signed by Fredman for Caucus.

15. In April 1985, Mitchell asked Fredman if the beneficiaries on Campaigner's November 26, 1984 notes could be changed. He said that could be done and they agreed that Campaigner's two notes (Exhibits 19 and 23) would be destroyed and that one new note would be issued in the principal amount of $15,000. Mitchell also agreed that the rate of interest could be reduced from 12 percent to 10 percent in the new note. Exhibit A. A short time later, a $15,000 note payable in one year with interest at 10 percent was mailed to her. Exhibit 24. Caucus was listed as the payor of that note

and it was signed by Fredman. The note was dated April 16, 1985 rather than November 26, 1984. Mitchell did not receive interest in the $15,000 loan between November 26, 1984 and April 16, 1985. did not agree to waive interest earned during that time, and did not authorize a change in the date of the two notes when they were rolled over and consolidated.

16. During the telephone conversation between Mitchell and Fredman on April 10, 1985, Mitchell agreed to make an additional loan to Caucus in the amount of $10,000. The loan was made in two separate payments to Caucus. A $6,000 payment was made by a check dated April 10, 1985 and a $4,000 payment was made to Caucus by a check dated April 26, 1985. On or about April 29. 1985. Caucus' $10,000 promissory note was mailed to Mitchell. The note. which was signed by Fredman, carried an interest rate of 10 percent and was payable in six months.

17. Apart from her loan to IDL, Mitchell loaned $40,000 to Caucus between July 1984 and April 29. 1985. As of November 21, 1985, only $2.000 had been repaid to her. A $1,000 payment was made late in April 1985, a $500 payment was made on November 6, 1985 and a $500 payment was made on September 30, 1985 (two checks).

18. During their telephone conversations in 19B4 and 1985, Mitchell and Fredman primarily talked about Caucus, but he never explained his relationship to Caucus, Campaigner or IDL. In addition, he never told her how they would repay the loans, if they had solicited loans from other persons, or if they had repaid those loans in a timely fashion.

19. All of Mitchell's loans to the Respondents. except the

$1,000 loan made to IDL, were made by check payable to Caucus. All the checks were presented for payment and paid by her bank. All the loans were solicited by Fredman. Mitchell had no direct contact with Greenberg and had very limited contact with Bettag. Her only contact with Bettag occurred in 1985 after she became concerned about the repayment of her notes. Bettag told her that the LaRouche organizations stand behind their commitments and that notes were good investments. Bettag explained that money wasn't coming in as fast as they had expected, but that all her loans would be repaid and that her money was safe.

20. After her conversation with Bettag, Mitchell advised family members about the loans she had made to the Respondents and the delinquencies that existed. Later, with their advice and input, she retained counsel and the Department was eventually informed of the transactions.

21. In late November of 1985, Joyce Rubenstein. a Caucus representative, telephoned Mitchell from New York to discuss her loans to Caucus. Rubenstein advised Mitchell that if she would make an additional $10,000 loan to Caucus she would be sure to get the rest if her money ($40,000) back. Based on these representations, Mitchell loaned Caucus another $10,000 for eight months at 12 percent. On November 29, 1985, Mitchell received confirmation from Caucus that the loan had been made under these terms. Confirmation was in a letter form. No note was issued as had been done in the past.

22. Mitchell considered all of her loans to the Respondents as investments, not unlike certificates of deposit that individuals can purchase from a bank. None of her loans were intended to be contributions and none of them were

collateralized. Apart from IDL's note. most of the notes issued were notarized by Bettag and most specifically stated that they could not be assigned. transferred or discounted. All of them were signed by Fredman.

23. In 1984 and 1985, the Respondents solicited loans from other Minnesota residents and from residents in other states including Illinois, Maryland, Alaska. Indiana and Washington.

24. No individual employed by or representing the Respondents gave Mitchell any financial information regarding the organizational Respondents that she could use to determine their ability to repay the loans she made. She was not told how the Respondents would be able to repay her loans. where the money used to repay her loans would come from. or what the risks of her investments were. Mitchell was not advised if Caucus was in default in its obligation to repay principal and interest to other investors or that one judgment had been entered against Caucus for failure to repay a loan when due. Moreover, Mitchell was never advised that the Respondents were not licensed to sell securities in the State of Minnesota or that the notes were not registered as required by law. In fact, Fredman told Mitchell that the loans were legal.

Based on the foregoing Findings of Fact. the Administrative Law Judge makes the following:

CONCLUSIONS

1. That the Minnesota Commissioner of Commerce and the Administrative Law Judge have authority to consider the

issues raised by the Commissioner's Cease and Desist Order and Order Suspending Exemption, as amended. under Minn. Stat. §§ BOA.21, 80A.15. subd. 3, and 14.50 (1984).

2. That the Department has complied with all relevant substantive and procedural requirements of law and rule and that the Respondents received proper and timely notices Xf the hearing and of the Commissioner's Orders.

3. That under Minn. Rule 1400.7300, subp. 5, the Department has the burden of proof to establish the statutory violations alleged by a preponderance of the evidence.

4. That the loans solicited by Ron Fredman and the notes issued by the organizational Respondents constituted offers and sales for purposes of Minn. Stat. § 80A.14, subd. 17 (1984X.

5. That the promissory notes offered and sold by the Respondents in the State of Minnesota constitute securities for purposes of Minn. Stat. § 80A.14. subd. 18 (1984)..

6. That the promissory notes offered and sold by the Respondents in the State of Minnesota were not registered with the Commissioner prior to or at the time of their offer of sale as required by Minn. Stat. § 80A.08 (1984).

7. That the Respondent Ron Fredman violated Minn. Stat. § 80A.014, subd. 1, by transacting business in this State as an agent without a license to do so.

8. That the organizational Respondents violated Minn. Stat. § BOA.04. subd. 2, by employing Ron Fredman as their agent.

9. That in connection with the sale of promissory notes to Mary Mitchell, the Respondents Ron Fredman and Ronald R. Bettag failed to state material facts necessary in order to make statements that were made not misleading, contrary to M1nn. Stat. § 80A.04, clause (b) (1984), by failing to disclose financial information which could have been used to determine the organizational Respondents' ability to repay the note$ when due and by failing to advise Mitchell that none of the Respondents were licensed to sell securities in the State of Minnesota and that the promissory notes were not registered pursuant to the Minnesota Securities Act.

10. That the Cease and Desist order proposed by the Commissioner is in the public interest and should be issued.

11. That under Minn. Stat. § 80A.15, subd. 4, the Respondents have the burden Xf proving any exemption claimed under Minn. Stat. § 80A.Ol to 80A.31 or any exception from a definition contained therein.

12. That the Respondents have failed to establish that the promissory notes they sold are subject to any exemption or exception.

13. That the Respondent Ron Fredman fraudulently misdated one of the promissory notes issued to Mitchell in violation of Minn. Stat. § 80A.Ol. clause (c) (1984).

14. That the Respondent Ron Fredman did not violate Minn. Stat. § BOA.Ol, clause (c) by telling Mitchell that some banks were falling.

Based on the foregoing Conclusions of Law, the Administrative Law Judge makes the following:

RECOMMENDATION

That the Cease and Desist Order and Order Suspending Exemption be made permanent.

Dated this 15th day of July, 1987,

JON L. LUNDE
Administrative Law Judge

Reported: Transcript Prepared.

MEMORANDUM

BURDEN OF PROOF

The Department argues that its only burden of proof on the question whether the Mitchell notes are securities is to show that the Respondents solicited loans from her and issued promissory notes reflecting the loans. It argues that the Respondents then have the burden to establish that the notes are not securities, citing Minn. Stat. § 80A.15. subd. 4 and Exchange National Bank v. Touche, Ross & Co., 544 F.2d

1126 (2d Cir. 1976). Under the cited statute. the burden of proving an exemption or an exception from a definition is upon the person claiming it. Hence. to the extent that the Respondents claim any statutory exemption or exception from a definition, they have the burden of proof. However, the Judge is not persuaded that the enforcement division's burden can be met merely by showing that the Respondents made a loan in this State and issued a note evidencing that loan. In Landreth Timber v. Landreth. 471 U.S. 681. 105 S. Ct. 2297, 85 L. Ed. 2d 692 (1985), the United States Supreme Court refused to hold that one could prove a security (note) simply by proving the document itself, which is exactly the result the enforcement division argues is appropriate. Moreover, under Minn. Rule 1400.7300. subp. 5. the Judge is persuaded that the Department has the burden of establishing that the notes were offered and sold as investments rather than commercial loans.

The definitions in the Minnesota Securities Act, like those in most securities acts[1] , apply "unless the context otherwise requires" Minn. Stat. § 80A.14, subd. 1. The courts have frequently cited this language to support departures from the literal definition of a security when required by the context in which the instrument alleged to be a security is offered or sold. See. e.g., Marine Bank v. Weaver, 455 U.S. 551, 556, 102 S. Ct. 1220, 71 L. Ed. 2d 409 (1982); Lino v. City Investing Co., 487 F.2d 689! 694 (3d Cir. 1973); State v. Hoephner, 574 P.2d 1079, 1081 (Okl. Cr. 1978). Although the courts have cited the "unless the context otherwise requires" language to avoid applying the securities definition literally, they generally have not held that the language was intended to change the normal burden of proof in civil or administrative proceedings and they have not held that that language

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[1] See 15 U.S.C. §78c(a)(10) and 77b(1) and the Uniform Securities Act of 1985, § (ULA 1987 Supp.).

constitutes an "exemption" or an "exception" that the Respondent has the burden to establish.

In Exchange National Bank, the court held that the statutory definition of a security should be applied literally and that persons seeking to avoid the plain language of the statute have the burden to establish that the context requires a different result. The literal test adopted in Exchange National Bank has been implicitly rejected by the United States Supreme Court. See United Housing Foundation, Inc. v. Forman, 421 U.S. 837, 849, 95 S. Ct. 2051. 2059, 44 L. Ed. 2d 621 (1975) and Landreth Timber Co. v. Landreth, supra, 105 S. Ct. at 2306 (1985). Moreover, it has apparently been rejected by every'See 15 U.S.C. § 78c(a)(lO) and 77 b(l) and the Uniform Securities Act of 1985. § 101 (ULA 1987 Supp.).other federal circuit court of appeals that has considered the issue. See. e.g., Hunssinger v. Rockford Business Credits Inc., 745 F.2d 484 (7th Cir. 1984); McClure v. First National Bank of Lubbock, 497 F.2d 490 (5th Cir. 1974), cert. den. 420 U.S. 930 (1975); Lino v. City Investing Co., supra. In addition, it has not been adopted in Minnesota. The Minnesota Supreme Court has always examined the economic reality of the instrument or transaction. See, e.g.. State v. Investors Security Corporation, 209 N.W.2d 405 (Minn. 1973). Recently it reaffirmed its preference for examining the context (economic reality). Rice County Specialized Tours, Inc. v.Hagen. 292 N.W.2d 520, 535 (Minn. 1986).

For all these reasons, it is concluded that the Department has the burden of establishing that the notes issued by the Respondents involved an investment rather than an ordinary commercial transaction and if such X showing is made. the note will constitute a security unless the Respondents can point to a specific statutory exemption or exception that applies to them.

The fact that the Respondents were precluded. by order, from presenting evidence showing that its notes are not securities is not equivalent to a default on that issue as the enforcement division has argued. When there is noncompliance with a discovery order, the Judge may order that certain facts be taken as established for purposes Xf the case, refuse to allow a party to support or oppose designated claims or defenses. or prohibit a party from introducing designated matters in evidence. Minn. Rule 1400.6700. subp. 3. In this case, the Respondents were precluded from opposing certain claims made by the Department. However, the Department was not granted a default judgment on those issues and it still has a burden of proof to meet. Consequently, the

Respondents' notes cannot be deemed to be securities under the theory that the Respondents are in default.

ARE THE PROMISSORY NOTES SECURITIES?

The first and most basic substantive issue that must be resolved in this case is whether the promissory notes Fredman sold to Mitchell for the organizational Respondents constitute securities. Minn. Stat. § 80A.14, subd. 18(a) defines a security as follows:

> "Security" means any note: stock; treasury stock; bond; debenture; evidence of indebtedness; certificate of interest or participation in any profit sharing agreement

In spite of the inclusive scope of the definition of a

security, the words used, including the words "any note"X cannot be literally applied. United Housing Foundation, Inc. v. Forman, supra. Instead. substance must prevail over form and the context in which an instrument is offered or sold must be examined to determine the economic reality involved. Tcherepnin v. Knight, 389 U.S. 332, 336, 88 S. Ct. 548, 553, 19 L. Ed. 2d 564 (1967). When the economic reality is that an investment rather than a commercial transaction is involved, the instrument will be treated as a security: otherwise, it won't. See, e.g.. Baurer v. Planning Group, Inc.. 669 F.2d 770. 775 (D.C. Cir. 1981). The Minnesota Supreme Court has not addressed the scope of the words "any note" and it has not adopted a test for determining when a note is a security. Consequently, the decisions of federal courts and other state courts and agencies must be consulted. This follows from the provisions of Minn. Stat. § 80A.31, which states:

Sections 80A.Ol to 80A.31 shall be so construed as to effectuate its general purpose to make uniform the law of those states which enact it and to coordinate the interpretation of sections 80A.Ol to 80A.31 with the related federal regulation.

See Specialized Tours, Inc. v. Hagen, supra at 535; Hayden v. McDonald, 742 F.2d 423. 428 (8th Cir. 1984).

Generally speaking, four tests have been adopted for determining when an instrument is a security: (1) the literal test. (2) the commercial/investment dichotomy test, (3) the risk capital test, and (4) the Howey test. However. there are variations to these tests and some basic principles that are always considered by the courts in determining what instruments are securities.

Although at least four different tests for determining when an instrument is a security have been adopted by the courts, the Judge is persuaded that the only appropriate test that should be used in determining whether a note is a security is the commercial/investment dichotomy test. The literal test articulated in Exchange National Bank of Chicago v. Touche Ross & Co., supra, has been implicitly rejected by the United States Supreme Court. In United Housing Foundation, Inc. v. Forman, 421 U.S. at 849, the court reiterated the need to examine the economic realities underlying a transaction and not the name attached to it, noted (footnote 14) that all but one of the Federal circuits that had recently considered the scope of the definition of a security had rejected a literal approach, and went on to examine the economic realities underlying the purchase of shares in a cooperative housing project to determine if they were securities. Subsequently, in Landreth Timber Co. v. Landreth, supra, the court did adopt a literal approach where stock is involved. but refused to do so for notes. The court stated. (105 S. Ct. 2306):

> . . . "note" may now be viewed as a relatively broad term that encompasses instruments with widely varying
> characteristics, depending on whether issued in a consumer context, as commercial paper, or in some other investment context. * * * We here expressly leave until another day the question whether "notes" or "bonds" or some other category of instrument listed in the definition might be shown "by proving [only] the document itself." * * * We hold only that "stock" may be viewed as being in a category by itself for purposes of interpreting the scope of the Acts' definition of "security."

In Landreth, the Supreme Court.said that instruments that bear both the name and all the usual characteristics. of stock present the clearest case for coverage by the plain language of the definition and should be treated as securities. Accordingly,

the court proceeded to apply the federal acts to the sale of 100 percent of the stock of a business. Although the United States Supreme Court has moved closer to the literal test generally applied by the Second Circuit. it strongly implied that the literal test is inappropriate in many situations and will be limited to stocks. In Specialized Tours, Inc. v. Hagen. supra. the Minnesota Supreme Court followed the Landreth decision but expressed dissatisfaction with it, noting that if it were writing on a "clean slate", it would have reached a different result by examining the economic realities xf the transaction. Since the Second Circuit's literal approach has not been accepted by the United States Supreme Court except in a modified version when stock is involved, and since the Minnesota Supreme Court has expressed dissatisfaction with it, it is concluded that the Commissioner should not apply that test in this case, even though it is discussed further below.

Also, the Judge is persuaded that application of the Howey test is inappropriate. The Howey test was adopted by the United States Supreme Court in SEC v. W.J. Howey Co., 328 U.S. 293 (1946) to identify "investment contracts" for purposes of the securities laws. The court described an investment contract as a transaction, contract or scheme whereby a person invests money or value in a common enterprise and is led to expect profits derived solely from the efforts xf the promoter or some third party. The First Circuit applied the Howey test to notes sold by a religious organization. SEC v. World Radio Mission,. Inc., 544 F.2d 535, 538 (1st Cir. 1976). However, it did not rely exclusively on Howey or explain why the Howey test was used. More important, other federal courts have rejected its use for any securities but investment contracts. In Landreth. the United States Supreme Court reaffirmed the fact that the Howey test was designed only to determine whether an investment contract constitutes a security. stating (105 S. Ct. at 2305):

> we would note that the Howey economic reality test was designed to determine whether a particular instrument is an "investment contract," not whether it fits within any of the examples listed in the statutory definition of "security" Our cases are consistent with this view. . Moreover, applying the Howey test to traditional stock and all other types of instruments listed in the statutory definition would make the Acts' enumeration of many types of instruments superfluous.

The Howey test has also been specifically rejected by several federal courts of appeals as an analytical tool for determining whether a note is a security. Hunssinger v. Rockford Business Credits, Inc., 745 F.2d 484. 492 (7th Cir. 1984); Exchange National Bank v. Touche Ross & Co.. supra: and Daily v. Morgan, 701 F.2d 496 (5th Cir. 19B3). Based in these cases, the Judge is persuaded that the Howey test is inappropriate for determining whether a note is a security and that test will not be discussed further.[2]

The risk capital test that has been adopted by the Ninth Circuit Court of Appeals is discussed below. even though the Judge is not persuaded that it should be used by the Commissioner in this case. It was rejected in Exchange National Bank, supra, and the Judge believes that the reasons

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[2] Even if the Howey test is used. the notes sold by Respondents would be ,/ securities under World Radio Mission. See also State v. Weisser, 161 N.W.2d 360 (N.D. 1968).

stated in that decision for rejecting the risk capital test are persuasive.

LITERAL TEST

Apart from the literal test for stocks adopted in Landreth. the literal test adopted in Exchange National Bank of Chicago v. Touche Ross & Co., supra, is the most inclusive test for determining whether a particular instrument is a security. In that case, the court held that the plain language of the federal statute should be closely followed and that notes should be treated as securities unless the context of the transaction clearly requires a different result. In discussing the kinds of notes that would not be included. the court referred to:

> the note delivered in consumer financing. the note secured by a mortgage on a home, the short-term note secured by a lien on a small business of some cf its assets. the note evidencing a "character" loan to a bank customer. short-term notes secured by an assignment of accounts receivable, or a note which simply formalizes an open-account debt incurred in the ordinary course of business (particularly if, as in the.case of the customer of a broker, it is collateralized)

Id. at 1138.

The inclusive. literal approach adopted in Exchange National Bank places a substantial burden on the issuer of notes to establish that the notes are required to be excluded from the definition. The burden placed on the issuer would apparently demand a clear showing that characterizing the

notes as securities would disrupt the settled expectations of both parties. interfere with routine transactions, provide additional protection where no such protection is needed,.or produce some other clearly undesirable result. See Petitioner's Post-Hearing Brief, Appendix 2, p. 19).

In this case. the notes Mitchell purchased do not bear any resemblance to the kinds of notes mentioned in Exchange National Bank as outside the scope of the securities laws. They are not the kind of routine loan transactions to which the securities laws should not apply and there is no evidence that the parties had any settled expectations regarding the status of the notes under the securities laws. In fact, Mitchell clearly regarded her loans as an investment similar to the purchase of certificates of deposit from a bank. Moreover, the loans Mitchell made appear to be the kind of transactions the securities laws were designed to cover and are the kind of investments that need the protections of the securities laws of this State. After all. Mitchell was unsophisticated in financial matters and incurred a significant risk without the ability to obtain and evaluate the information needed to make an informed investment decision. For these reasons, it is concluded that the notes sold to Mitchell constitute securities under the literal test.

RISK CAPITAL TEST

The "risk capital test" was devised by the California Supreme Court in Silver Hills Country Club v. Sobieski, 55 Cal. 2d 811, 13 Cal. Rptr. 186, 361 P.2d 906 (1961). It is not an appropriate test for determining the status of an instrument as a security in all cases. United Housing Foundation, Inc. v. Format, supra. 421 U.S. 837 at 857 n. 24. However, in Great Western Bank & Trust v. Kotz. 532 F.2d 1252 (9th Cir. 1976). the Ninth Circuit used the risk

capital test to determine whether the notes involved in that case were securities. Generally speaking. the ultimate inquiry under the risk capital test is whether the lender contributes "risk capital" that is subject to the entrepreneurial or managerial efforts of the borrower. In determining if it is, the duration of the loan, the amount of collateralization, the circumstances of issuance, the relationship between the amount borrowed and the size of the borrower's business, and the contemplated use of the proceeds must all be considered. Because the loans Mitchell made were not collateralized. because her loans and the loans other persons made to the Respondents were not discrete transactions--but part of a general offering made in a number cf states--and because the notes were not short-term-demand-notes. it is concluded that the notes are securities under the Kotz test. Clearly, Mitchell placed her capital at risk and was totally dependent upon the Respondents' efforts for payment.

Commercial/Investment Dichotomy Test

At least four federal circuits have adopted the commercial/investment dichotomy test for determining what notes constitute securities. See CNS Enterprises, Inc. v. G x G Enterprises. 508 F.2d 1354 (7th Cir. 1975): Baurer v. Planning Group, Inc. supra Lino v. City Investing Co., supra: and Bellah v. First National Bank, 495 F.2d 1109 (5th Cir. 1974). Under this test, the protection of the securities laws is confined to investors and not to borrowers and lenders in commercial settings. Thus, in determining whether a particular note is an investment, the courts examine the economic reality of the note to determine whether it was offered or sold as an investment. In this case, the Judge is persuaded that the notes sold by the Respondent to Mitchell constitute securities. In determining that the Respondents' notes were purchased as an investment and not as an incident to a commercial loan, the following factors.were considered:

a. whether the lender is a bank, financial institution or commercial lender in the business of making loans or a private party;

b. whether the notes were issued in connection with a consumer installment transaction or the purchase or real estate;

c. whether the notes were collateralized;

d. whether the sales took place outside the normal markets for notes and commercial paper;

e. whether the sales to Mitchell were an isolated set of transactions or part of a broader solicitation of loans from members of the public;

f. whether the proceeds of the loan were used to provide capital needed to finance a business or to purchase consumer goods and services.

g. the fact that notes are within the plain language of the definition of a security.

Consideration of these factors persuades the Administrative

Law Judge that the notes Mitchell purchased from the Respondents were bought as an investment. She considered her loans to be investments not dissimilar from the purchase of certificates of deposit from a bank. Moreover, Mitchell is not a typical commercial lender. Unlike a bank or other financial institution, she is not in the business of making loans, and the loans she made were not made in connection with a consumer installment transaction and they were not secured with any collateral. Likewise, they took place outside the normal markets for notes and commercial paper, and they were not an isolated transaction, but part of a broader solicitation of loans from members of the public. Although the loans paid a fixed rate of interest. the rate paid was higher, in some cases. than the rate Mitchell was receiving from her bank. Given the purposes of the securities law to protect members cf the public from fraud and imposition, and due to the lack of any commercial aspect to the notes. it is concluded that the notes sold by the Respondents were not of a commercial nature and that they constitute securities under the commercial/investment dichotomy test.

Treating the notes the Respondents sold to Mitchell as securities is consistent with the purposes of the Minnesota Securities Act, which is to regulate the merits xf securities in order to protect the public against fraud and imposition. State v. Investors Security Corporation. 209 N.W.2d 405, 408 (Minn. 1973). The Minnesota courts have consistently held that the securities laws should not be given a narrow construction. Sex, e.g.. Donovan v. Dixon, 113 N.W.2d 432. 443 (Minn. 1962). The Minnesota Supreme Court's expansive view of the securities laws has led to a consistent broadening of their coverage. State v. Investors Security Corporation. supra at 409. Treating the notes Respondents sold to Mitchell and other residents is consistent with the remedial purposes of the act and is necessary in order to

protect citizens of this State from fraud and imposition.

In determining when an instrument is a security, it is appropriate to consider the character given to the instrument in commerce by the terms of the offer, the plan of distribution and the economic inducements made by the offeror. Marine Bank v. Weaver, 445 U.S. 551. 556. 102 S. Ct. 1220 (1982). In this case, the Respondents represented its notes as investments, planned to sell notes throughout the State of Minnesota and other states in order to accumulate capital for a variety of unknown purposes. and held out economic inducements to Mitchell to purchase those notes. Those inducements included flexible maturity dates and competitive interest rates. There is no reason why the Respondents' notes should not be treated as they were represented to be. The solicitation of members of the general public seeking a passive return from their capital and the sale to them of units of a larger offering are the hallmarks of an investment transaction. Hunssinger v. Rockford Business Credits, Inc., supra at 492. In the enforcement of the securities act, it is not inappropriate that promoters' offerings be judged as being what they are represented to be. SEC v. C.M. Joiner Leasing Corp., 320 U.S. 344. 352-53, 64 S. Ct. 120, 124, 8B L. Ed. BB (1943). In this case, the Respondents represented their notes as investments and they should be treated as such for purposes of the Minnesota Securities Act.

The mere fact that Respondents' instruments are called promissory notes is some evidence that they were intended to be covered by the securities act. While the name given to an instrument is not dispositive. it is not wholly irrelevant to a decision as to whether it is a security. As noted in United Housing Foundation, Inc. v. Forman, supra, 421 U.S. at B50-51. there may be occasions when the use of a name that appears in the definition of a security will lead a purchaser to

justifiably assume that the securities acts will apply. Although there is no evidence that Mitchell had any specific understanding that the securities acts would apply because the instruments were called notes, it is still appropriate to treat the notes as securities given the fact that they are called notes and contain the hallmarks of an investment transaction. Cf. Landreth Timber . v. Landreth, supra, 105 S. Ct. at 2306.

The Respondents argue that the notes they sold bear a fixed rate of interest and that the repayment of principal plus a fixed rate of interest does not constitute an expectation of profits under the Howey test. As mentioned before, it is not appropriate to apply the Howey test to notes purchased from an issuer by an investor. The Howey test may be appropriately applied when the investor takes a commercial note and packages it in some other form of investment contract. See. e.g., State v. Investors Security Corporation. supra. Marine Bank v. Weaver, supra. However, that was not done in this case. Notes and bonds are included in the definition of a security and ordinarily the return on an investment in those notes and bonds is in the form of interest. Consequently, as noted in Hunssinger. the mere fact that the Respondents' notes bore a fixed rate of interest is immaterial.

The Respondent also argues that the notes the Respondent sold are not securities due to the nature of the Respondent organizations. stating (Post-Hearing Brief. p. 18).

> These are not the usual investment transactions conducted by organizations and individuals interested only in making a profit on their business. Both the lenders and the recipients of the funds in these transactions were motivated by.certain firm social and political

> beliefs. These beliefs were the reason the loans were made to the Respondents, rather than an expectation of profit. Simply, the loans were made to support the Respondent organizations in their social, political and economic activities, not in a profitable business enterprise.

This argument is not supported by facts in the record. Although Mitchell said she would not loan money to the Respondents if she disagreed with their political and social goals, she was not willing to make substantial contributions (more than $25.00) to them in support of those goals and objectives. She invested money in their notes only because she considered them to be good investments that would be repaid with interest. Furthermore, when the issuer xf securities is not engaged in commercial activity, there may be a greater need for regulation because there will be no "profits" that can be used to repay a note. Rather, repayment will depend on the contributions or loans of third parties. The risks of such an enterprise are substantial.

Treating the organizational Respondents' notes as securities is consistent with the decision in Securities and Exchange Commission v. World Radio Mission, Inc.. 544 F.2d 535 (1st Cir. 1976) and the decisions of the Securities Commissions in California, Alaska, and Maryland. In World Radio Mission, the First Circuit Court of Appeals found that notes sold by a religious organization to members of the public were securities. The defendant in that case was a religious organization engaged in worldwide evangelical activities. It proselytized its beliefs through a radio program and by the publication and distribution of pamphlets, magazines and books. In order to establish a religious community in New England and to finance its other activities. the religious

organization raised funds through two types of investment plans. The investment plans involved the sale of interest-bearing notes. originally, the notes were issued in amounts of not less than $1,000 demoninations and were payable in seven years with interest at eight percent and with a 90-day notice acceleration clause. Later, there were variations in the notes that were sold with increased minimum amounts and interest as high as 12 percent. Sometimes there was no early withdrawal-of-principal feature. A second loan plan involved five-year $10,000 notes paying 9% interest with a bonus of an acre of land at the organization's New England community. The court found that the notes sold by World Radio Mission fell squarely within the literal language of the securities acts and the interpretive tests developed by the Supreme Court and specifically found that the religious motives of the investors were irrelevant because the notes were sold as investments to believers and nonbelievers alike. Id. at 539. In finding a security, the court cited the Joiner test that instruments should be judged by the character the instrument is given in commerce and by what they are represented to be, and concluded that they were represented to be investments. The same is true here. An investment involves the "placing of capital or laying out of money in a way intended to secure income or profit from its employment." Howey, 328 U.S. at 298. The notes sold to Mitchell were represented as good investments, she considered them to be good investments. and they should be treated as investments under the securities laws. Doing so is consistent with relevant court decisions, the decisions reached by other state agencies, and Minn. Stat. § 80A.31.

The most important issue raised by the Respondents concerns the constitutionality of applying the securities laws to political organizations under the First Amendment. The Respondents argue that the Minnesota Securities Act. as applied to them, is overly broad and impermissibly imprecise for purposes of the First Amendment because its application

will impair their rights of expression, association and privacy when there is no significant public interest justifying the impairment. Neither the Administrative Law Judge nor the Commissioner has authority to declare an act of the Legislature unconstitutional. Starkweather v. Blair. 71 N.W.2d 869, 884 (Minn. 1955); Quam v. State, 391 N.W.2d 803, 809 (Minn. 1986); Neeland v. Clearwater Memorial Hospital, 257 N.W.2d 366, 368 (Minn. 1977). However, to the extent that a statute must be construed, constitutional principles may be considered by the Administrative Law Judge and the Commissioner in an appropriate case. Jackson Cty. Education Ass'n v. Grass Lake Community, 291 N.W.2d 53 (Mich. App. 1980).

First Amendment freedoms are not absolute. Buckley v. Valec, 424 U.S. 1 (1976); Bates v. City of Little Rock, 361 U.S. 516, 523 (1960). however, government action which curtails First Amendment freedoms must be closely scrutinized, must be supported by a compelling or overriding governmental interest, and must be closely or narrowly drawn. Buckley v. Valeo. supra. When associational and privacy rights come in conflict with state interests, the compelling needs of the government will justify the restrictions if they are, in balance, more important. and are the least restrictive means of accomplishing the government's stated objectives.

The organizational Respondents' position is that the State has no compelling interest to regulate its notes and that the State's regulations will deprive it of its First Amendment rights. They argue, without support in the record, that compliance with the State's securities laws may be prohibitively expensive and might be impossible because the statutes are incompatible with the operations of political organizations. Respondents note, for example, that political organizations do not have set issues of securities or a series of

securities and that they do not issue notes with uniform interest rates or due dates. Moreover, since they continuously raise funds, registration would require them to set specific times to begin and end fundraising and flexibility in the terms of the notes they issue would be virtually impossible to obtain. Respondents also argue that statutory earnings requirements and minimum capitalization restrictions on fund use and vagueness about the required promotional materials that must be filed create insurmountable constitutional problems. In the Respondent's view, the Commissioner cannot monitor the viewpoints of political associations and organizations. The Respondents also point out that political associations' fundraising activities frequently concern current issues which change daily and that it would be virtually impossible to define the offerings or promotional materials in such a circumstance. Moreover, the Respondents argue that the broker/dealer and agent disclosure requirements of the securities laws are completely incompatible with the First Amendment. and that the prospectus requirements alone will make it impossible for a political association to comply with disclosure requirements. They point out that listing its promoters will impair associational rights requiring disclosure of active supporters. Based upon the problems compliance with the securities act may create for political organizations and the extent to which First Amendment rights may be abrogated or impaired, Respondents conclude that the securities act should be limited to commercial or business enterprises and not to political associations, and that if political associations are to be covered. the statute must be rewritten and substantially clarified.

The Respondents' arguments are based on the United States Supreme Court's decision in FEC v. Massachusetts Right to Life,U.S. , 107 S. Ct. 616 (1986). In that case. the Supreme Court decided that Section 316 of the Federal Election Campaign Act is unconstitutional as applied to nonprofit corporations formed to promote political ideas

because it infringed upon protected speech without a compelling justification.

The record does not contain much information about the Respondents. For example, IDL's status as an independent association and as a campaign committee for purposes of-the federal election laws has been.admitted-cut has not been proven. Similarly, while a copy of Caucus' original Articles cf Incorporation is in the record, there is no evidence that the Articles originally.filed have not been amended and no evidence that the limitations in those.-Articles have been followed.- Therefore.the Judge.does not know if monies Caucus obtains are used for political purposes only or whether they have been used for the benefit of particular individuals or business ventures. Moreover, there is no evidence in the record concerning Campaigner and the relationship between Campaigner and Caucus and how funds collected by these organizations are interchanged. commingled or spent. Assuming, however, that it is true that all the organizational Respondents were formed solely to disseminate political ideas rather than to amass capital, and assuming that has been their sole function, the Judge is not persuaded that the Massachusetts Right to Life decision prohibits treating the Respondents' notes as securities. That case simply held that restrictions on the spending of some nonprofit corporations were unconstitutional. It did not state that nonprofit corporations formed to disseminate political ideas can borrow money and issue notes free of any state or federal regulation.

The State's securities law is designed to protect the public from fraud and deception in transactions involving securities, to prevent losses from investments in worthless enterprises, and to protect credulous and incompetent persons from their own inclinations to speculate in hazardous enterprises. State v. Gopher Tire & Rubber Co., 146 Minn. 52. 177 N.W.2d

937 (1920); Bond v. Charlson, 374 N.W.2d 423 (Minn. 1985). These are compelling interests. In Larson v. Valente, 456 U.S. 228, 248. 102 S. Ct. 1673. 1685 (1982), the United States Supreme Court recognized that states have "a significant interest in protecting its citizens from abusive practices in the solicitation xf funds for charity. and that this interest retains importance when the solicitation is conducted by a religious organization." Previously. in Cantwell v. Connecticut, 310 U.S. 296, 306, 60 S. Ct. 900. 904. the court suggested that organizations may not commit frauds upon the public under the cloak of religion. Thus. in World Radio Mission. supra, the court rejected an argument that the securities issued by religious organizations were subject to First Amendment protection. The court held that since sales were solicited from the general public and since the purchases were not contributions made with no real expectation of recovery, but investments made for the secular purpose of obtaining a profit, that they were securities subject to Federal law. The notes said by the organizational Respondents, like the notes sold by world Radio Mission, were offered to the general public as investments. not contributions. While Respondents may have a First Amendment right to spend their money as they wish and to promote whatever political purposes and goals they desire, they do not have a First Amendment right to solicit money in any manner that they desire or to avoid any and all laws governing the sale of securities simply because they have political goals. The Judge is persuaded that the State's interest in preventing fraud authorizes the State to require political and social organizations to register their securities and, if necessary. to file the economic brochures and prospectuses that those groups intend to use to sell them; that is, that regulation is not per se unconstitutional. That does not mean that the Commissioner can review the truthfulness of the political positions of such associations, but he can review the truthfulness and completeness of the economic facts that pertain to the security. Therefore, it is concluded that there is no prohibition from entry of the Cease and Desist order

proposed by the Department. Resolution of any other more specific constitutional problems, in the Judge's view, must be resolved on a case-by-case basis after development of a complete record.

FRAUD

The Department has charged the Respondent, Ron Fredman. with the violation of Minn. Stat. § 80A.Ol, clause (c), by telling Mitchell that some banks were failing and by misdating a promissory note rolled over in April 19B5. Section 80A.Ol states, in part:

> It is unlawful for any person, in connection with the offer, sale or purchase of any security, directly or indirectly:
>
> (b) to make any untrue statement of material fact or omit to state material facts necessary in order to make the statements made, in light of the circumstances under which they are made, not misleading; or
>
> (c) to engage in any act, practice, or course of business which operates or would operate as a fraud or deceit upon any person.

For purposes of section 80A.Ol, fraud and deceit are not limited to common law deceit. The intent to defraud is irrelevant. Aaron v. SEC, 446 U.S. 680. 697, 100 S. Ct. 1945. 1956 (1980). Therefore, the focus of the law is the

effect of the violation on the public. Van Duyse v. Israel, 486 F. Supp 1382, 1387 (E.D. Wis. 1980). Fredman's statement during the course of his conversations with Mitchell that some or many banks were failing was not shown to have misled Mitchell and was not shown to be untrue. Mitchell at no time believed that her banks were in trouble or that her bank deposits were unsafe, and she knew her bank deposits were insured. Furthermore, it was not even shown that Fredman's statements were made in the course of selling notes to her. rather than in the course of describing the policies. goals and political objectives of the LaRouche organizations. Consequently, it is concluded that the enforcement division has failed to establish that those statements constitute an act, practice or course of business which operated as a fraud upon Mitchell. However, the Judge is persuaded that the Respondents! use of current dates whenever notes were rolled over without making any provision for prior interest payments did constitute an act. practice or course of business that acted as a fraud upon her for purposes of the statute. Although Respondents submitted the affidavit of Ronnie Y. Fredman denying any intent to deprive Mitchell of this interest, the Judge does not find the affiant's statements regarding the rollover note of April 16, 1985 to be persuasive or believable.

The Judge is also persuaded that the Respondents Ronald R. Bettag and Ron Fredman failed 10 state material facts necessary in order to make statements that were made not misleading contrary to the provisions of Minn. Stat. § 80A.Ol(b) by failing to disclose financial information which Mitchell could have used to determine the organizational Respondents' ability to repay the loans she made to them and by telling Mitchell that the loans were legal when the notes were not registered with the Commissioner and Fredman and Bettag were not licensed to sell them. For purposes of the statute. misstated or omitted facts are material if there is a substantial likelihood that a reasonable person would consider

it important in deciding whether to buy a security or if there is a substantial likelihood that the disclosure of the misstated or omitted fact would have been viewed by the reasonable investor as having significantly altered the "total mix" of the information made available. TSC Industries, Inc. v. Northway, Inc., 426 U.S. 438 (1976). Although the record does not clearly state how the organizational Respondents hoped to repay Mitchell's loans, if they did, information regarding the source of the funds to be used for repayment and the Respondents' ability to repay those notes would certainly have been important. substantial and material to a reasonable investor's decision to purchase the notes. Bettag and Fredman's statements that the loans were legal and that her investments were safe were certainly misleading without providing her with specific information regarding their financial position and ability to repay. Therefore, the Judge is persuaded that the statute was violated in this case.

J.L.L.

IN THE CIRCUIT COURT OF COOK COUNTY, ILLINOIS

COUNTY DEPARTMENT - LAW DIVISION

DONALD E. FROELICH
Plaintiff
vs
NO: 86 L 17562

CAUCUS DISTRIBUTORS, INC., CAMPAIGNER PUBLICATIONS
INC., SCHILLER INSTITUTE, INC., PAUL GREENBERG,
RONALD BETTAG, and certain unnamed JOHN and JANE DOES, Individually and as agents and employees of affiliates,
Defendants

ORDER

This cause coming to be heard on motion of Defendant, RONALD BETTAG to dismiss Count 1 through and including Count IX of Plaintiff's Complaint pursuant to Code of Civil Procedure X2-615, all parties with due notice, the Court having reviewed the pleadings, and memoranda and argument of counsel, and the Court making findings of law:

(a) Count 1 insufficiently pleads civil conspiracy to commit fraud as to Ronald Bettag;

(b) Count I1 insufficiently pleads breach of contract as to Ronald Bettag;

(c) Counts 111, IV, V, VI, VII and VIII fail to allege facts which establish alleged loans by Plaintiff to any party to be "securities" as contemplated by Illinois Sec. Law of 1953, 111. Rev. Stat. Ch. 121-1/2, X137.1 et.seq. and the Court finds that Plaintiff cannot allege any fact or set of facts to allege a cause of action under said statutes;

(d) Count IX fails to allege facts which establish alleged loans by Plaintiff to any party to be consumer or business or commerce transactions as contemplated by Illinois Consumer Fraud and Deceptive Busines. Practices Act, Ill.Rev.Stat. Ch. 121-1/2, X261 et. seq. and the Court finds that Plaintiff cannot allege any fact or set of facts to allege a cause of action under said statutes;
and the Court being fully advised:

IT IS HEREBY ORDERED:

1. Count 1 of Plaintiff's Complaint is stricken. Plaintiff is given leave to file Amended Count 1 within 28 days.

2. Count 11 of Plaintiff's Complaint is stricken. Plaintiff is given leave to file Amended Count 11 within 28 days.

3. Counts III, IV, V, VI, VII and VIII of Plaintiff's Complaint founded on Illinois Securities Law of 1953,Ill.Rev.Stat.Ch. 121-1/2, X137.1 et. seq., are dismissed.

4. Count IX of Plaintiff's Complaint, founded on Illinois Consumer Fraud and Deceptive Business Practices Act, Ill.Rev.Stat.Ch. 121-1/2, X261 et. seq. is dismissed.

DATE: _____ ENTER:

JUDGE

Attorney X20468
LAW OFFICES OF
STEIN & ROTMAN
105 W. Madison - Suite 605
Chicago, Illinois 60602
236-5375

IN THE CIRCUIT COURT OF COOK COUNTY, ILLINOIS
COUNTY DEPARTMENT - LAW DIVISION

DONALD FROELICH
Plaintiff, -vs-
No. 86 L 17562
CAUCUS, et al.,
Defendants.

REPORT OF PROCEEDINGS had at the hearing of the above-entitled cause, before the Honorable THOMAS E. HOFF!XAN, Judge of said court, on Thursday, the 7th day of January, A.D., 1987.

PRESENT:
MR. LONNY BEN OGUS,

appeared on behalf of the Plaintiff;

STEIN & ROTMAN, by:
MR. ORIN S. ROTMAN,
appeared on behalf of the Defendant.

Cecilia A. Peterson, CSR,
Official Court Reporter
Circuit Court of Cook County
Law Division

THE CLERK: Froelich versus Caucus. MR. ROTMAN: Good morning, your Honor. Orin Rotman, representing the defendant, Patag.

MR. OGUS: Lonny Ben Ogus, representing the plaintiff, Donald Froelich.

MR. ROTMAN: I will make my comments very short since 7 the Court has had all the pleadings. This is defendant's motion to strike Counts I through and including IX for failure to state a cause of action or in the alternative a mc,re definite statement.

There are two factual allegations made with regard to Ronald Patag. One is that he was agent of some undetermined corporation, one of and/or three corporations. The other allegation is in an affidavit which is in Exhibit C to the complaint wherein Mr. Patag is alleged to have had a conversation with the plaintiff in January or February of 1986 regarding post-due promissory notes.

Count I of the complaint does not incorporate the affidavit, Exhibit C, so the only allegation as to Mr. Patag is that he was the agent of one of the three corporations or maybe all of them. That does not engage him as a conspirator for fraud.

Count two is for breach of contract. There is no contract alleged against Mr. Patag. There are promissory notes executed by different entities. There is no contract of personal

undertaking in the conversation set forth in paragraph 13 of Exhibit C.

Count III through VIII are based on statutory actions by the allegation based on conduct between September 1984 and December 1984. The only allegation by Mr. Patag is conversation of January and February 1986, no action which could come within the purview of the statute of the allegations in Counts III to VIII.

Count IX under fraud and deceptive business practices, clearly that is not under the items previously stated because also these are political loans for election campaign set forth by plaintiff in his affidavit and have no relationship to business transactions whatsoever.

MR. OGUS: Very simply, your Honor, this was a pattern of acts of the LaRouche group to get my client to give them money with the intention of never repaying it. He gave him $78,000, goes through serious machinations to take his money without his consent on some occasions, with his consent on some occasions, but with certain promises that they would repay it. They didn't tell him what they were doing with it and things like that.

Defendant, Patag, the only defendant before this Court at this time, is alleged to be an agent representative of the three groups, Caucus, Campagner and Schiller. And the complaint affidavit talks about being asked by Mr. Patag to do certain things concerning the loans that he had already given to those corporations and what he would do if he did certain things and things like that.

Very clearly this is a fraud. We allege fraud and particularly in a fraud situation one co-conspirator is liable for all the acts of the other co-conspirator as long as they know

what is going on.

THE COURT: You never pled a cause of action in civil conspiracy. That is separate and apart from fraud. It is a separate count. You have him on Count I -- separate fraud, that he committed the fraud. It becomes apparent from the allegations in Count I. You haven't pled all of the elements of the cause of action for fraud against this defendant. I know where you're going. You want to allege civil conspiracy and want to make him responsible for that, which Greenberg did, and all the rest of them did That's fine, but you have to plead civil conspiracy. Unless you plead civil conspiracy that they acted in concert, intending to achieve a given result, 21 although each one of them may have done a separate part of the fraudulent scheme, you haven't got a cause of action against them. Just because he is an agent and representative of corporations that may have defrauded your client arguably, unless you can allege he is the one that committed the fraud he is not, as an agent, liable for the fraud of his principal.

MR. OGUS: What we're saying, he was part and parcel of the whole scheme.

THE COURT: Fine. Where did you say that? Where is that? Where is the cause of action for conspiracy?

MR. OGUS: On number 21.

THE COURT: The bare allegation that defendants were part of the scheme to induce plaintiff to lend money and obtain access to plaintiffs CMA?

MR. OGUS: That is what they did.

THE COURT: There is nothing wrong with inducing someone to lend money to another unless the lending of the money is done under fraudulent circumstances. It has !7 to be a conspiracy to commit fraud. It has to be a conspiracy to do it by illegal means.

MR. OGUS: 17 and 18 I believe we pled both of those.

THE COURT: Which defendant?

MR. OGUS: All of them were acting together. One does it, one makes a call one time, another one makes a call another time.

THE COURT: Unless you set up the elements of the cause of action for civil conspiracy Count I does not state a cause of action. By using the phrase defendants, without describing who you're talking about doesn't say the issue which you have sufficiently laid out that it was Greenberg who solicited the loans and didn't tell plaintiff the funds were being received by a corporate defendant. Schiller is the one who withdrew money from a cash management account. You don't allege that Patag did any.of these things. If you want to allege he was involved in a civil conspiracy allege it and plead it. Count I is stricken.

As to Count II, for breach of contract, he is not a party to this contract and if it's intended to be some oral contract between him and the plaintiff then that particular case I would refer you to Martin Trigona versus Bloomington, 101 Ill. App. 3d. 943. That will tell you what must be pled in order to state a cause of action for breach of contract. And mere base allegations that there was an offer, there was an acceptance and there was consideration without more is insufficient to state a cause of action for breach of oral contract.

There must be factual allegations to support those X3 conclusions of law and there aren't any here, not as against this defendant. Certainly he's not a party to this unsecured promissory note. His name doesn't appear anywhere on it. By the terms of these contracts, and I presume these contracts are promissory notes that you exhibit, and the oral contract set out by his affidavit, I don't see any breach of contract here. I am going to strike that one. If you want to replead it, go ahead.

As to the Counts III through VIII, based on Illinois Security Law, Illinois Security Law deals with securityregulations including registration of dealers and sellers engaged in selling securities, contains certain anti-fraudand penalties. A security must be involved in the alleged cause of action. 2.1 specifically says:

> "Security means any note, stock, treasury stock, bond, debenture, evidence of indebtedness, certificate of interest or participation in any profit-sharing agreement, collateral-trust certificate, preorganization certificate or subscription, transferable share, investment contract, investment fund share, face amount certificate, voting trust certificate, fractional undivided interest in oil, gas, or other mineral lease, right or royalty, option, put, call, "privilege, indemnity or any other right to purchase or sell a contract for the future delivery of any commodity offered or sold to the public and not on a registered contract market, or, in general, any interest or instrument commonly known as a security, or any certificate of deposit for, certificate of

interest or participation in, temporary or interim certificate for, receipt for, guarantee of, or warrant or right to subscribe to or purchase any of the foregoing."

CHAPTER 121-1/2, 137.2-1.

"A security within the Illinois Security Law and Federal Securities Act is a contract, transaction or scheme whereby one person invests his money in a common enterprise on the theory that he expects to receive profits solely from the efforts of the other.

Hoffer versus Lorrie, 552 Ill. App. 29, was denied at 86 Supreme Court 237:

"In determining whether an instrument is a security within Illinois Securities Law or the Federal Securities Act the Court looked at the substance of the transaction, the relationship between the parties, elements of control as against the form of the instrument."

Here the substance of plaintiff's nine count complaint was a loan made to a political campaign of Mr. Lyndon A. Larouche, allegedly loans were to be made "-- and funds collected from the federal government as !3 national collection funds, totaled about $9,000, to be 1X paid in three years with 14 percent interest.

Despite your allegation the loan name Larouche campaign is not a securities law. An enterprise is not involved in a business sense. Plaintiff did not make an investment with an

expected return as the terms are commonly used. All he did was loan some money and expect some interest on it. If this falls within the securities law then every promissory note issued by any person that contains an interest rate falls within the securities law and it simply does not. These are not securities as within the means of our securities law.

The Illinois Consumer Fraud and Deceptive Business Practices Act will authorize you to pursue a cause of action for deceptive commercial conduct. You have to have a deceptive act of practice relied on and a deception must occur. But in reviewing the private rights of action the Courts are guided by the terms of Section 11 (a) of the statutes which expressly provides that the action be literally construed to effect its purpose.

Here the deceptive practice complained of is omissions of material facts involving repayment of money with interest, matching election funds, payment of funds in the event of illness or catastrophe, etcetera. In all, plaintiff claims defendant falls within the act and they solicited loans or investments or contributions from Illinois residents which constitute unfair or deceptive acts of practice within the meaning of the act. But you must be a consumer or borrower or businessman in order to have standing to bring an action under our Consumer Fraud and Deceptive Business Practices Act.

Consumers are persons who purchase, make purchases or contract for purchase of merchandise not for resale in the ordinary course of business, but for use in their household. Their term trade or commerce is advertising for sale or sale for distribution of services, property tangible or intangible, real, personal or business, any other article, commodities or anything of value, wherever situated, directly or indirectly

affecting people of this state.

Plaintiff hasn't alleged any facts to illustrate that this cause for deceptive activity falls within the parameters of our act. Plaintiff has not shown he is a consumer of any kind. He has not shown that the defendant is engaged in the trade or commerce or profession unless one would suggest that conducting political activity is a trade or commerce. Nothing has occurred within a trade or commerce.

I don't see any violation of the Illinois Consumer Fraud and Deceptive Business Practices Act which has been pled here. In sum total I am going to strike Counts I and II. Counts III through IX, I am not only striking I am dismissing with a finding there was no posit of facts in spite of plaintiffs complaint that would entitle them to relief under either our securities law or in the alternative under Consumer Fraud and Deceptive Trade Practices. That will be the order. (Which were all the proceedings and in the above-mentioned cause.)

IN THE CIRCUIT COURT OF COOK COUNTY, ILLINOIS
COUNTY DEPARTMENT - LAW DIVISION

Ithe Honorable THOMAS E. HOFFMAN, Judge of the Circuit Court of Cook County, presiding judge at the hearing of the aforementioned cause, do hereby certify that the above and foregoing is a true and correct Report of Proceedings had at the said hearing.

AND, FORASMUCH, THEREFORE, as the matters and things hereinbefore set forth do not otherwise fully appear of record, the attorney for the tenders this Report of Proceedings and prays that the same may be signed and sealed by the judge of this court pursuant to the statute in such case made and provided.

WHICH IS ACCORDINGLY DONE

this ____ day of _____, 1988.

HONORABLE THOMAS E. HOFFMAN

Circuit Court of Cook County, Illinois

IN THE CIRCUIT COURT OF COOK COUNTY,
ILLINOIS COUNTY DEPARTMENT - LAW DIVISION

I, CECILIA A. PETERSON, an Official Court Reporter for the Circuit Court of Cook County, County Department/Law Division, do hereby certify that I reported in shorthand the proceedings had at the hearing in the above-entitled cause; that I thereafter caused the foregoing to be transcribed into typewriting, which I hereby certify to be a true and accurate transcript of the proceedings had before the Honorable THOMAS E. HOFFMAN, Judge of said court.

Official Court-Reporter

Dated this 12th day
of January, 1988.

STATE OF MICHIGAN
COURT OF APEALS

HARRY W. AGNSORGE, CLAUDE BOONE, CARL BOONE, GORDAN BUGAI, JULIUS BUGAI, DONALD CARLSON, RUDOLPH CARLSON, OSCAR CHRISTIANSON, STANLEY CHRISTIANSON, JAMES ECKERLE, GEORGE FREDERICKSON, FREDERICKSON FARMS, JAMES HOPKINS, HOWARD HUNT, MARTIN JELINEK, JOHN KILCHERMAN, GERTRUDE KIMMERLY, JEROME KOLARIK , JULIUS KOLARIK SR., JULIUS KOLARIK JR., LARS LEE, WHITNEY LYON, MORK & SONS, A Michigan co-partnership, KENDALL PROBST, SHERWOOD PROBST, LEWIS RANGER, JOSEPH SHIMEK, EMILY NASH SMITH, NORA SWENSON, CHARLES VAN PELT, RONALD J. VONHOLT, conducting business as VONHOLT FARMS, GARY WATSON AND LINTON WATSON,

Plaintiffs-Appellants/Cross-Appellees,

-v-

DAVID R. KELLOGG, DOROTHY JANE KELLOGG, RAY ELLSWORTH KELLOGG and GERALD THOMAS STEIN, jointly and severally,

Defendants-Appellees/Cross-Appellants.

BEFORE: Cynar, P.J., E.A. Weaver and J.H. Hausner* , JJ.

PER CURIAM

Plaintiffs appeal by right from a Grand Traverse Circuit Court judgment of no cause of action in favor of defendants.

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* Circuit judge, sitting on the Court of Appeals by assignment.

Defendants claim a cross-appeal from the same judgment. We affirm

The Traverse City Canning Company (TCCC), a Michigan corporation, operated a fruit processing and canning business for approximately fifty years. The company went bankrupt in 1982. Defendants are the officers, directors and shareholders of the bankrupt corporation. Plaintiffs are commercial cherry growers who had business dealings with the TCCC over the years.

According to the testimony adduced at trial, a typical plaintiff, upon the harvest of his cherries, would deliver the fruit to the TCCC for processing, The plaintiff did not receive immediate payment for his crops. Instead, the grower received a weigh ticket a a receipt. About thirty days after harvest, the typical plaintiff would receive a statement from the TCCC showing the amount owing to the grower after taxes. The amount owning constituted the balance of th grower's account. Commonly, partial payment was made by the TCCC at that time. Subsequent payments by the TCCC were generally made upon the request of the grower. Growers commonly left their money in their growers' accounts, which were interest bearing accounts. It was established at trial that these dealings were typical of industry-wide practices.

In 1979, the TCCC suffered significant financial losses due to high interest rates and poor harvest yields. As a result, the TCCC concluded that it would be unable to make full payments on the growers' accounts if same was demanded by the growers. Consequently, in November, 1981, the TCCC mailed to each grower that grower's account statement and a promissory note.

Plaintiffs had not requested the October, 1981 promissory notes; plaintiffs did not negotiate with the TCCC with regard to the terms of he notes. The issuance of the promissory notes was a unilateral act on the part of the TCCC.

Thereafter, on February 2, 1982, the TCCC petitioned for Chapter XI reorganization under federal bankruptcy laws. As a result of the bankruptcy proceedings, plaintiffs did not receive the amounts owed to them by the TCCC. Plaintiffs, therefore, filed the instant action seeking to impose personal liability on defendants under the Michigan Uniform Security Act (MUSA), MCL 451.801 (1), and that, therefore, the MUSA was inapplicable. Moreover, specifically as to the notes issued to Emily Nash Smith and Julius Bugai, the trial court found that those plaintiffs had made bona fide loans to the TCCC; thus, those transactions came within the exception to the MUSA found in §401(j) (6) (A). On appeal, plaintiffs challenge these findings as clearly erroneous.

We are first asked to determine whether the promissory notes issued by the TCCC and the growers' accounts maintained by the TCCC were "securities" within the meaning of the statutory provision. In making this determination, we do not write on a clean slate. Well-settled principles enunciated by the appellate courts of this state establish that the notes and evidence of indebtedness received by plaintiffs were not procured for purposes of speculation and investment and, therefore, do not fall within the ordinary concept of a security.

Section 301 of the MUSA, MCL 451.701; MSA 19.776 (301), makes it unlawful for any person to offer or sell any security in the state unless it is registered under the act of the security or the security or transaction was exempted under §402. The purpose of this statutory restriction on th offer or

sale of securities is to protect the public against fraud and deception in the issuance, sale, exchange or disposition of securities. People v Dempster, 396 Mich 700, 704; 242 NW2d 381 (1976). As a matter of judicial policy, the act should be broadly construed to effectuate this purpose. Id.

The word "securities" is defined in §401 (1) as follows:

"'Security' means any note; stock; treasury stock; bond; debenture; evidence of indebtedness; certificate of interest or participation in any profit-sharing agreement; collateral-trust certificate; preorganization certificate or subscription; transferable share; investment contract; voting-trust certificate; certificate of deposit for a security; certificate of interest or participation in an oil, gas, or mining title or lease or in payments out of production under such a title or lease; or, in general, any interest or instrument commonly known as a 'security', or any certificate of interest or participation in, temporary or interim certificate for, receipt for, guarantee of, or warrant or right to subscribe to or purchase, any of the foregoing. 'Security' includes any contractual or quasi contractual arrangement pursuant to which: (1) a person furnishes capital, other than services, to an issuer; (2) a portion of that capital is subjected to the risks of the issuer's enterprise; (3) the furnishing of that capital is induced by the representations of an issuer, promoter, or their affiliates which give rise to a reasonable understanding that a valuable tangible benefit will accrue to the person furnishing the capital as a result of the operation of eh enterprise; (4) the person furnishing the capital does not intend to be actively involved in the management of the enterprise in a meaningful way; and (5) a promoter or its affiliates anticipate, at the time the capital is furnished, that financial gain may be realized as a result thereof..."

We reject at the outset any suggestion that the present transaction, memorialized by the issue of "notes" and "evidence of indebtedness," must be considered a security transaction simply because the statutory definition of security includes the words "any note...[or] evidence of indebtedness." Rather, we adhere to the basic principles that have guided the appellate courts in this state in their decisions in this area.

In general, the courts that have interpreted Michigan's security statutes have been careful to look beyond the form of the transaction to its substance, paying special attention to the economic realities of the situation. People v Breckenridge, 81 Mich App 6, 16-17; 264 NW2d 99 (1978), lv den 402 Mich 915 (1978); Dep't of Commerce v DeBeers Diamond Investment Ltd, 89 Mich App 406, 409-410; 280 NW2d 547 (1979), lv den 406 Mich 998 (1979). Whether a particular transaction must be considered a security transaction depends upon the statutory language, the real nature of the transaction, and the real intent and purpose of the parties, looking beyond labels and devices. People v Blankenship, 305 Mich 79, 85-86; 8NW2d 919 (1943); Breckenridge, supra; Prince v Heritage Oil Co., 109 Mich 198, 197; 311 NW2d 741 (1981); Moffit v Sederlund, 145 Much App 1, 15; 378 NW2d 491 (1985) lv den 425 Mich 860 (1986).

In Breckenridge, supra, this Court considered the applicability of the MUSA to a transaction involving promissory notes. The Court noted that the salient feature of a securities sale under the MUSA is the public solicitation of venture capital to be used in a business enterprise. The Court, quoting with approval from Bronstein v Bronstein, 407 F Supp 925, 930 (ED Pa, 1976), then opined:

"'The question whether a note constitutes a covered security depends on whether the note was procured for purposes of speculation or investment or for purposes of making a commercial loan. As a matter of policy, this distinction is a valid one. The federal securities laws are designed to protect investors, not persons engaged in ordinary consumer or commercial loan transactions * * *. Thus courts have restricted application of the Acts to those notes procured for investment and have excluded notes issued in the context of a commercial loan transaction." Breckenridge, supra, 15-16.

With these general principles in mind, we return to the language of §401 (1). We read the expressly enumerated factors set forth in §401 (1) to constitute the factors to be considered i determining the investment character of a transaction. In the context of a "note" or "evidence of indebtedness" these factors would aid th court in distinguishing an investment or securities transaction from a loan transaction. From our review of the record, we find that the trial court properly used these factors to determine the investment character of the transaction.

We also conclude that the trial court's finding that the notes and accounts did not constitute securities within the meaning of $401 (1) was not clearly erroneous. Trial testimony established that plaintiffs' accounts arose as a result of industry-wide practices regarding the dealings between growers and independent fruit processors. Each grower had the option to request payment of all or any part of his or her account balance from the TCCC. Any portion of the balance which remained with the TCCC bore interest at fixed rate and, therefore, the return to plaintiffs was not dependent on the profit made by the TCCC. The promissory notes issued to plaintiffs in October, 1981, were merely a consolidation of the

plaintiffs' account balances through 1980. The return promised on these notes was premised on a rate of interest and not on the profits of the TCCC. Finally, the testimony of individual plaintiffs demonstrated that they understood the nature of the transaction with the TCCC as a loan rather than as an investment.

We are next asked to determine whether the trial court clearly erred when it found that plaintiffs Julius Bugai and Emily Nash Smith had made "bona fide loans" to the TCCC and, therefore, that the transactions were not security transactions governed by the MUSA.

The terms "offer" and "sale" are defined in §401 (j). Section 401 (j) (6) (A) specifically excludes "any bona fide loan" from the definition of these terms.

The record establishes here that the promissory notes issued to Smith and Bugai were given in change for cash. Bugai testified at trial that he intended to make a loan to the TCCC. These fact coupled with the fact that the notes were interest bearing at a fixed rate, and return did not depend on the profits of the TCCC, indicates that the transactions were loans rather than investments. Accordingly, we conclude that the trial court did not clearly err in finding as fact that Smith and Bugai had made bona fide loans to the TCCC.

On cross-appeal; we are asked to determine whether the trial court erred in denying an award of attorney fees to defendant pursuant to MCR 2.403

A party is liable for the opposing party's attorney fees under MCR 2.403 (o) only if the party has rejected the evaluation and the verdict is less favorable to the rejecting party (by more than ten percent) than the mediation evaluation.

In the instant case, plaintiffs rejected the May 15, 1985 mediation evaluation. Defendants accepted same. We, however, find that the mediators issued no valuation which could be accepted or rejected by the parties. While the mediators did find that defendants were liable to plaintiffs, they left the issue of damages open and invited the parties to submit additional material on the issue. Both parties to submit additional material on the issue. Both parities accepted this invitation. The mediators failed to place a value on plaintiffs' damages prior to the trial. Accordingly, the May 15, 1985 mediation evaluation presented no settled decision. Thus because plaintiffs might have accepted the mediation valuation if they had not expected further action as to the issue of damages, we conclude that it would be unfair to subject plaintiffs to eh penalty provisions of MCR 2.403 (o).

Defendants also ask us to determine whether the trial court clearly erred when it found that defendants Dorothy Jane Kellogg, Ray Ellsworth Kellogg and Gerald Thomas Stein had failed to meet the burden imposed upon them by MCL 451.810(b); MSA 19.776(b). Because we have determined that the trial court correctly found that the instant transaction was not governed by the MUSA, we declined to make such a determination.

Defendants' remaining issues were not addressed by the trial court. We, therefore, decline their review. People v Turner, 123 Mich App 600, 604; 332 NW2d 626 (1983).

Affirmed

/s/ Walter P. Cynar
/s/ Elizabeth A. Weaver
/s/ John H. Hausner

August 26, 1986
Dear DFLer,

I enthusiastically support Ray Stock in his bid to upset Bill Frenzel.

Ray has a big task ahead of him, and he needs you help. First, he must defeat a LaRouche disciple-Stanley Bentz-in the primary, and then take on the entrenched Bill Frenzel.

Ray needs you to vote in the Primary on Sept 9. We must show the nation that Minnesota will not tolerate the La Rouche fringe. Ray intends to see that what happened in Illinois does not happen here.

Ray needs you to knock on doors, make telephone calls, lick stamps, drop literature, and write letters to the editor. He already has an active group of more than 150 volunteers, but more are needed. Ray will work hard.

Ray also needs your dollars. He can't match Frenzel's war chest stuffed with PAC dollars; but your contribution of $35, $50 or $100 will make a difference. Ray will use your money wisely.

Ray Stock is a man of deep conviction and compassion. He was moved to challenge Bill Frenzel because of Frenzel's callous contra aid vote. For Ray it was just one more example of Frenzel's disregard for what is right and his blatant disregard fo the views of the people of the Third District.

> Once again, Bill–the media "moderate"–has voted on both sides of the issue; and when the vote counted, Frenzel was on the wrong side– the Reagan side.

Ray believes the security of his two little girls and of all our children depends not on MX missiles, Star Wars defense systems and a $300 billion defense budget, but on hard-headed negotiations, finding new and creative ways to solve conflict, and on finding our common humanity. He believes education is the key to our future. He believes that clean air and clean water are our birthright and that the federal government has the responsibility to see that our environment is safe and clean. And he believes that our deficit-ridden-buy now, pay later-economy is a poor legacy to leave our children.

Ray believes, and I believe, that Bill Frenzel has not and will not provide the leadership we need to solve these problems. Ray Stock will.

Ray knows that beating Bill Frenzel will be difficult. But in a short time he has put together an impressive, well, organized campaign. Ray's energy, enthusiasm, and conviction are contagious. When people tell Ray that Bill Frenzel can't beat, he tells them: "Don't bet on it."

Tim Penny proved the experts wrong in 1982. Ray Stock plans to do the same in 1986.

But to upset Bill Frenzel. Ray needs your help. He needs you to:

VOTE SEPTEMBER 9: Stanley Bentz must be soundly defeated;

VOLUNTEER: call 927-9298 to see how you can help;

CONTRIBUTE: you get tax credits for your contributions.

Ray needs and deserves our support. With your help we can put Ray Stock in Congress.

Best regard,

/s/ Hubert Humphrey, iii

Attorney General

P.S. On September 3, please join me at an open house for Ray. It will be at the Stock for Congress campaign headquarters at 4005 West 65th Street, Suite 223, in Edina. The time is from 5:00 p.m. to 8:00 p.m. I hope you can come. It will be a great chance to get to know Ray.

FILED
NOV 23 1988
JOSEPH F. SPANIOL, JR.
CLERK

No. 88-628

IN THE

Supreme Court of the United States

October Term, 1988

CAUCUS DISTRIBUTORS, INC., and CAMPAIGNER PUBLICATIONS, INC., New York Corporations, INDEPENDENT DEMOCRATS FOR LAROUCHE, an unincorporated association, RON FREDMAN, RONALD R. BETTAG, PAUL GREENBERG, and all other parties and organizations acting in concert with the named Petitioners,

Petitioners,

vs.

MINNESOTA COMMISSIONER OF COMMERCE,

Respondent.

ON PETITION FOR WRIT OF CERTIORARI
TO THE COURT OF APPEALS OF MINNESOTA

RESPONDENT'S BRIEF AND APPENDIX IN OPPOSITION

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QUESTIONS PRESENTED FOR REVIEW

1. Should the Court review a decision by a state court holding that an organization claiming First Amendment status which solicits investments from the public is subject to state securities laws?

2. Does the federal election campaign law immunize federal election campaign committees from the duty to comply with generally applicable state securities laws?

3. Should the Court review a decision of a state administrative law judge imposing sanctions on Petitioners for refusing to provide the names of persons who may be investors even though the state had shown a compelling state interest and was subject to a strict confidentiality order?

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IN THE

Supreme Court of the United States

October Term, 1988

No. 88-628

CAUCUS DISTRIBUTORS, INC., and CAMPAIGNER PUBLICATIONS, INC., New York Corporations, INDEPENDENT DEMOCRATS FOR LAROUCHE, an unincorporated association, RON FREDMAN, RONALD R. BETTAG, PAUL GREENBERG, and all other parties and organizations acting in concert with the named Petitioners,

Petitioners,

vs.

MINNESOTA COMMISSIONER OF COMMERCE,

Respondent.

ON PETITION FOR WRIT OF CERTIORARI
TO THE COURT OF APPEALS OF MINNESOTA

BRIEF IN OPPOSITION TO PETITION FOR WRIT OF CERTIORARI

Respondent Minnesota Commissioner of Commerce respectfully requests that this Court deny the Petition for Writ of Certiorari seeking review of the Minnesota Court of Appeals opinion in this case. That opinion is reported at 422 N.W.2d 264 (1988) and is reproduced in Appendix C to the Petition.

JURISDICTION

Petitioners invoke the jurisdiction of this Court solely under 28 U.S.C. § 1254(1). (Petition at 2.) That statute, which relates to cases in the federal circuit courts of appeals, does not furnish this Court with jurisdiction to review the decision of a state court. Accordingly, Petitioners have not provided this Court with a jurisdictional basis to grant the relief they seek.

STATEMENT OF THE CASE

This proceeding was commenced by the issuance of a Cease and Desist Order, Notice of Right to Hearing and Order Suspending Exemption by the Minnesota Commissioner of Commerce ("Respondent" or "Commissioner") on June 4, 1986. An Amended Cease and Desist Order was issued on July 17, 1986. Respondent's Appendix at RA-1.[1] The Amended Cease and Desist Order alleged that Petitioners[2] sold unregistered securities through unlicensed agents in the State of Minnesota and alleged various acts of fraud and failure to disclose material facts.

On July 15, 1987, the Administrative Law Judge ("ALJ") issued proposed Findings of Fact, Conclusions and Recom-

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[1] Matters in Respondent's Appendix will hereinafter be cited as "RA" followed by the page number identifying the document.

[2] Petitioners are Caucus Distributors, Inc. (hereinafter "CDI"), Campaigner Publications, Inc. ("CPI"), Independent Democrats for LaRouche ("IDL"), Ron Fredman ("Fredman"), Ronald R. Bettag ("Bettag"), and Paul Greenberg ("Greenberg"). CDI, CPI, and IDL are sometimes collectively referred to herein as "the organizational Petitioners" and Fredman, Bettag and Greenberg as "the individual Petitioners."

mendation together with an extensive memorandum. (App. F.) The ALJ concluded that the loans and notes offered by Petitioner Fredman were offers to sell securities under the Minnesota Securities Act, Minn. Stat. ch. 80A (1984) ("Blue Sky Act"). He concluded that Petitioners violated the provisions of the Blue Sky Act concerning registration of securities and agents and failed to disclose material facts as required by the Act. He also concluded that Respondent Fredman violated the anti-fraud provision of the Act.

On September 3, 1987, Respondent Minnesota Commissioner of Commerce issued Findings of Fact and Conclusions of Law and Order which are virtually identical to the recommendation of the Administrative Law Judge. Petitioners secured review of Respondent's decision by the Minnesota Court of Appeals which affirmed it on March 30, 1988. The Minnesota Supreme Court denied a petition for further review on June 10, 1988.

The Hearing

A hearing was held before the ALJ on August 4-5, 1986. Mary Mitchell, who had loaned various sums of money to two of the organizational Petitioners and who had received promissory notes evidencing these loans from the organizational Petitioners, was the only person to testify. Mrs. Mitchell, an elderly widow with a high school education, testified that she invested in excess of $40,000 in the organizational Petitioners because they offered her higher interest rates than she was making on certificates of deposit and because of their representation that her investment would be safe. Although she was sympathetic to some of the views advanced by Petitioners, her primary motive in advancing the $40,000 was to make a

profitable and safe investment. (TR-44, TR-57). She refused to contribute any amounts to Petitioners in excess of $25 (TR-111, 118). The Department[3] also introduced into evidence enforcement proceeding documents from other states which alleged that Petitioners were soliciting investments from elderly members of the public in those states.

Background of Order of Preclusion

The ALJ found that a satisfactory record regarding Petitioners' activities could not be made without further discovery and continued the hearing. (RA-8.) There were several additional continuances because of discovery disputes. On January 27, 1987, the ALJ granted the Department's motion to preclude Petitioners from contesting certain allegations in the Amended Cease and Desist Order because of their refusal to comply with material portions of the ALJ's discovery orders. (RA-51.) The events which led to the ALJ's preclusion order will be discussed in the following paragraphs.

In June and July, 1986, the Department served various discovery requests on Petitioners. The Department sought, *inter alia*, the names and addresses of persons in Minnesota who had invested in the organizational Respondents. Petitioners raised various objections to the discovery, including First Amendment claims, and did not respond to material portions of the discovery.

The Department sought discovery of the names and addresses of persons in Minnesota who had invested in the organizational Petitioners for two reasons. First, many courts

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[3] The party appearing in support of the Amended Cease and Desist Order during the administrative hearings was the Enforcement Division of the Minnesota Department of Commerce. It is referred to herein as "the Department."

which apply the commercial/investment dichotomy test in determining if a note is a security have focused on the scope of the offering. The Department sought this information in order to show that the transactions with Mrs. Mitchell were not an isolated phenomenon. Second, the Department needed this information to rebut Petitioners' isolated sales exemption claim. See Minn. Stat. § 80A.15, subd. 2(a) (1984).

Contrary to Petitioners' assertions, the Department never contended that all notes are securities under Minnesota law. The Department did not seek to apply the Minnesota securities law to persons whose primary purpose in loaning money to Petitioners was to support their political or social goals. The Department maintained, however, that the securities law should apply to investors such as Mrs. Mitchell who, while they may have been in sympathy with Petitioners' goals, were induced to loan money through representations concerning the profitability and security of investing in Petitioners and whose primary purpose was to make a profitable investment.

On October 6, 1986, the ALJ issued a discovery order. (RA-13.) That order required that each organizational Petitioner provide certain information to the Department concerning the identities of persons who made loans to the organizational Petitioners or, in the alternative, provide the ALJ with lists of all Minnesota residents who had made loans to the Petitioners, the ALJ then choosing at random the names of 30 persons from each list and providing them to the Department. Finally, the ALJ issued an order permitting limited discovery (RA-13). He also issued a protective order which applied to all discovery which Petitioners claimed was subject to First Amendment protections (RA-13). In a memorandum attached to the protective order, the ALJ balanced the First Amendment rights of Petitioners with the com-

pelling state interest of the Department in conducting discovery. The Petitioners did not comply with the discovery order.

At October 24, 1986, the Department moved for an order of the ALJ precluding Petitioners from contesting certain allegations in the Amended Cease and Desist Order. (RA-40.) These were the allegations which the Department might have been able to prove through the testimony of persons whose identities were to be disclosed pursuant to the ALJ's Order of October 6, 1986, but were not disclosed. On December 2, 1986, the ALJ denied the Department's request for preclusion or other sanctions because he believed the Petitioners' noncompliance was due, in large part, to the seizure of their business records by state and federal authorities in Virginia. (RA-44.)

At or about this time, Petitioners furnished the Department with the names and addresses of seven persons in Minnesota who had loaned money to them. The Department then renewed its complaint about discovery to the ALJ. It argued that Petitioners had selectively provided it with only the names of persons whose loans were not made as investments. It also contended that the other 40 persons whose names were not disclosed might well fit Mrs. Mitchell's profile as a person whose primary intent was to make an investment.

On December 15, 1986, the ALJ issued another discovery order. (RA-48.) The ALJ directed Petitioners to provide the Department with various information concerning Minnesota residents to whom offers or sales of promissory notes had been made and who had not requested anonymity and, as to persons who had requested anonymity, to provide the information to the ALJ who would then randomly select 25 percent of the names of those individuals and accompanying data

and provide it to the Department's counsel. The protective order required the Department to maintain strict confidentiality. The ALJ also indicated that noncompliance with the order would result in the imposition of sanctions including preclusion of the presentation of evidence.

On December 23, 1986, counsel for Petitioners wrote to the ALJ advising that his clients would not disclose any names of Minnesota residents to whom it had offered promissory notes. On January 17, 1987, the ALJ issued an order denying a request for an interlocutory appeal of his discovery order, rescheduling the continued hearing to a date certain, and permitting Petitioners an opportunity to submit written argument addressing the propriety of the sanctions proposed by the Department. (RA-51.)

On January 27, 1987, the ALJ issued an order imposing sanctions for noncompliance with discovery. The order precluded Petitioners from contesting the last sentence in paragraph 1 and paragraphs 2 and 7 of the Amended Cease and Desist Order. (RA-51.)

REASONS FOR DENYING THE PETITION

The special and important reasons set forth in Rule 17 of this Court which might support granting of a petition for a writ of certiorari are lacking here. The issues were fully considered and correctly decided below. Petitioners have cited no federal or state court decisions which are in direct conflict with the rulings below. Moreover, although various issues of federal law are raised, neither the record nor existing precedent supports Petitioners' claims.

I. THE MINNESOTA SECURITIES ACT APPLIES TO PETITIONERS' INVESTMENT PROGRAM.

Petitioners initially argue that the Minnesota courts erred in determining that their notes were securities because, in balancing the various factors, the Minnesota courts failed to give due weight to their First Amendment status. They do not attack the constitutionality of the Blue Sky Act as applied to them. Assuming, *arguendo*, that Petitioners are organizations which espouse political ideas and are entitled to special First Amendment protection, this argument is nothing more than a challenge to the interpretation of a Minnesota statute by a Minnesota court because it attacks only the balancing process. This is purely an issue of state law. This Court, of course, should not grant certiorari to review an issue of state law.

Even if their argument is construed as an attack on the statute as applied, review should not be granted because the factual record does not support Petitioners' claims. Petitioners called no witnesses and ignored the administrative subpoenas served on them by the Department. Their assertions that they are First Amendment political organizations have virtually no support in the record. There was no testimony that the loans were used to further First Amendment purposes. The Administrative Law Judge who heard the case found that the complaining witness invested over $40,000 in CDI because she viewed it as a profitable investment.

In any event, First Amendment freedoms are subject to restrictions when a compelling government interest supports the restriction. *Buckley v. Valeo*, 424 U.S. 1 (1975); *Bates v. City of Little Rock*, 361 U.S. 516, 523 (1960). This Court has recognized the existence of such a compelling state interest in the application of a charitable solicitation law to a religious

organization, *Larson v. Valente*, 456 U.S. 228 (1982). Organizations may not commit a fraud on the public in the cloak of religion. *Cantwell v. Connecticut*, 310 U.S. 296 (1940). When investments are made for the purpose of obtaining a profit as a result of general public solicitation, the First Amendment offers no shield from the application of securities laws. *Securities and Exchange Comm'n v. World Radio Mission, Inc.*, 544 F.2d 535 (1st Cir. 1976).

Petitioners' "parade of horribles" on pp. 11-15 of their Petition demonstrates why the investments which they offered to the complaining witness *should be* within the power of the states to regulate. Petitioners have countless other alternatives available to them to raise money, including solicitation of contributions and the sale of literature. However, if Petitioners wish to raise funds by offering profit-making investments to the general public with promises of safe and lucrative returns, as was the case with the complaining witness here, then prospective investors *should* have the right to know that the soliciting organizations "do not have large capital assets," "do not tend to accumulate capital," and have made claims which "do not turn out to be factual." Petition at 11.

II. THE FEDERAL ELECTION CAMPAIGN ACT AMENDMENTS OF 1974 DO NOT PREEMPT STATE BLUE SKY LAWS.

Petitioners contend that the Federal Election Campaign Act Amendments of 1974, Pub. L. Nos. 93-443, 88 Stat. 1263, reprinted in 1974 U.S. Code Congressional and Admin. News 1436, *et seq.*, Election Campaign Amendments of 1974, preempt Minnesota's Blue Sky Law with respect to loans made to it. The relevant portion of the law provides:

> The provisions of chapter 29 of Title 18 United States Code, relating to elections and political activities, and preempt any provisional state law with respect to election of federal office.

2 U.S.C. § 453 (1985).

Petitioners assert that the Minnesota Blue Sky Law is preempted by this provision even though the Blue Sky Law is a law of general application rather than a "provision of state law with respect to election of federal office."

The preemption issue arises from a unique factual situation. The complaining witness made various investments in CDI and received various promissory notes in return. Some of the promissory notes bore the name of IDL, a federal election campaign committee.[4] Respondent knows of no other instance in which a federal election campaign committee has made a general solicitation of loans as investments from the public. This appears to be solely relevant to the practices of IDL. Since most preemption issues are likely to involve the relationship of federal and state *election* laws, review of the issue by this Court is unlikely to produce a decision which will shape the development of the law in the area of preemption.

IDL faces a heavy burden in arguing preemption. As this Court has noted, "[t]he goal of any preemption inquiry is 'to determine the congressional plan.'" *[illegible] v. Rehner*, 463 U.S. 713 (1983), quoting *Pennsylvania v. Nelson*, 350 U.S. 497 (1956). In making that inquiry, " 'we start with the assumption that the historic police powers of the States were not to be superseded by Federal Act unless that was the clear and manifest purpose of Congress.' " *Jones v. Rath Packing*

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[4] The complaining witness apparently wrote out one check for $1,000 directly to IDL at the direction of CDI. (TR-45.)

Co., 430 U.S. 519 (1977), quoting *Rice v. Santa Fe Elevator Corp.*, 331 U.S. 218 (1947). "This assumption provides assurance that 'the federal-state balance' [citation omitted] will not be disturbed unintentionally by Congress or unnecessarily by the courts." *Id.*

Accordingly, it is well settled that " 'an unexpressed purpose to nullify. . . [state power] is not lightly to be attributed to Congress.' " *California Retail Liquor Dealers Ass'n v. Midcal Aluminum, Inc.*, 445 U.S. 97, 103-104 (1980), quoting *Parker v. Brown*, 317 U.S. 341, 351 (1943). "Preemption of state law by federal statute or regulation is not favored 'in the absense of persuasive reasons—either that the nature of the regulated subject matter permits no other conclusion, or that Congress has unmistakably so ordained.' " *Chicago & N.W. Transp. v. Kalo Brick & Tile Co.*, 450 U.S. 311, 317 (1981), quoting *Florida Lime & Avocado Growers, Inc. v. Paul*, 373 U.S. 132, 142 (1963). Where possible—as it is here—"the proper approach is to reconcile 'the operation of both statutory schemes with one another rather than holding one completely ousted.' " *Merrill Lynch, Pierce, Fenner & Smith v. Ware*, 414 U.S. 117, 127 (1973), quoting *Silver v. New York Stock Exchange*, 373 U.S. 341, 357 (1963).

Petitioners quote from *Louisiana Public Service Comm'n v. F.C.C.*, 106 S. Ct. 1890 (1986) summarizing the situations in which preemption can occur. However, none of the various situations where preemption may occur as set forth in *Louisiana Public Service Comm'n* are present here. They will be discussed in the remainder of this section.

Congress in enacting the 1974 amendments did not express any intent to preempt all State law as it may apply to campaign committees. Congress clearly intended to preempt most state laws specifically dealing with election matters. However,

Petitioners suggest no authority for the proposition that Congress intended to preempt laws of general application outside the area of elections, such as the law at issue, insofar as they may apply to a federal election campaign committee.

Indeed, despite the seemingly absolute preemption of state *election* laws as they may relate to federal elections, the Conference Committee which enacted section 104 stated that it "does not affect state laws as to the manner of qualifying as a candidate, or the dates and places of elections." S. Rep. No. 93-689, 93rd Cong., 2d Sess. 1974, *reprinted in* 1974 U.S. Code Cong. and Admin. News 5668. The Committee explained further that:

> The provisions of the conference substitute make it clear that Federal Law occupies the field with respect to criminal sanctions relating to sources of campaign funds used in Federal races, the conduct of Federal campaigns, and similar offenses, but does not affect the States' rights to prohibit false registration, voting fraud, theft of ballots, and similar offenses under State law.

S. Rep. No. 93-689, 93rd Cong., 2d Sess. 1974, *reprinted in* 1974 U.S. Code Cong. and Admin. News at 5587, 5638. If preemption of election-related laws was not complete, preemption of laws of general application outside the area of elections certainly was not intended.

A further reason to reject preemption is that there is no outright or actual conflict between federal and state law. The 1974 federal statute was enacted:

> to impose overall limitations on campaign expenditures and political contributions; to provide that each candidate for Federal office shall designate a principal campaign committee; to provide for a single reporting responsibility with respect to receipts and expenditures

> by certain political committees; to change the campaign expenditures and political contributions; to provide for public financing of Presidential nominating conventions and Presidential primary elections; and for other purposes.

Pub. L. No. 93-443, 88 Stat. 1263-1304, codified as amended at 2 U.S.C. §§ 431-455. The Minnesota Blue Sky Act does not conflict with these purposes in any way; its focus is on unsound investments. The public purposes served are different but complementary, and effectuation of one does not hinder the other.

Compliance with both federal and state law is possible. If a federal campaign committee chooses to offer securities to the investing public, it can comply with both the registration and notification requirements of the Minnesota law and the federal election law.

Congress clearly could not have intended to exempt federal campaign committees from state laws of general application outside the election area because the scope of the federal enactment is so limited. Federal law requires that a committee have a treasurer and governs accounting practices, reporting of contributions and financial records, 2 U.S.C. § 432, registration, 2 U.S.C. § 433, and general reporting requirements, 2 U.S.C. § 434-435. There are no other restrictions or limitations on what a committee may do. The focus of the federal election law is on the political process—the public's right to know the sources of a candidate's funding, limitations on campaign expenditures and public financing. Obviously, a federal election campaign committee could violate many state laws of general application such as tort law, commercial law and the like. There is nothing in the federal law concerning protection of third parties who may be injured by the activities of cam-

paign committees. There is no reason to immunize campaign committees from the application of state laws because the committees are federally constituted.

Congress has not legislated comprehensively, thus occupying the entire field of regulation. Congress had not legislated comprehensively with respect to election law let alone with respect to other matters of general application such as state security laws. Congress has made no attempt to cover all matters which may in one way or another relate to federal campaign committees.

The Blue Sky Act does not stand as an obstacle to the accomplishment and execution of the full intent of congress. Enforcement of the Minnesota Blue Sky Act as to federal campaign committees which choose to sell securities will not hamper the accomplishment of congressional intent on elections in any way. The state court was therefore correct in rejecting Petitioners' preemption argument and the issue does not warrant this Court's review.

III. THE ALJ'S ORDER PRECLUDING PETITIONERS FROM CONTESTING CERTAIN ALLEGATIONS OF THE AMENDED CEASE AND DESIST ORDER BECAUSE OF THEIR REFUSAL TO COMPLY WITH HIS DISCOVERY ORDERS DID NOT VIOLATE THEIR CONSTITUTIONAL RIGHTS.

The ALJ's order precluding Petitioners from introducing evidence challenging certain allegations in the Amended Cease and Desist Order is a discovery order in which he balanced the conflicting interests of the parties. (RA-55.) Petitioners admit that he was entitled to balance the interests, Petition at 20, but ask this Court to second-guess his decision. The issue is so dependent on the particular procedural and factual

circumstances of this case that it is unsuitable for review by this Court. Moreover, an administrative law judge's decision on discovery is entitled to great deference by appellate courts. Two appellate courts have already reviewed the ALJ's decision without disturbing it and there is no reason for this Court to repeat that exercise.

The ALJ's Order precluding Petitioners from contesting certain allegations of the Amended Cease and Desist Order was justified by the Department's compelling interest in obtaining the information and did not violate Petitioners' constitutional rights. The Department commenced this hearing on the basis of a complaint by a single Minnesota investor. The Department attempted to obtain the names and addresses of Petitioners' other Minnesota investors (or a representative sampling of the investors) from Petitioners, both before and after the commencement of the proceeding. Petitioners admit that there are at least 48 such persons but, in response to the Department's interrogatories and the ALJ's orders, produced but seven names and addresses, which they selected themselves.

The Department was seriously prejudiced by Petitioners' failure to provide these names and addresses, or at least a representative sampling of them, as required by the ALJ's orders. First, the information was necessary to rebut Petitioners' isolated sales exemption claim. *See* Minn. Stat. § 80A.15, subd. 2(a) (1985 Supp.).[5] Petitioners point to nothing in the record supporting their contention that they aban-

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[5] Minn. Stat. § 80A.15, subd. 2(a) (1985 Supp.), exempts isolated sales, provided that no person shall make more than ten sales of securities of the same issuer in a 12-month period, and provided further that in the case of an issuer, the sales are not advertised for sale to the public through a program of general solicitation by mail or telephone.

doned this claim before the ALJ issued his order of preclusion. They cannot because they did not. Second, the information sought by the Department was important to show that Petitioners were engaged in widespread solicitation of the public to raise money. Under the "commercial/investment dichotomy test" which was adopted by the Minnesota Court of Appeals, App. C 16-17, this is a factor in determining whether or not a note is security and the facts and circumstances of the offering are critical. Indeed, this was very important information.

The right to privacy in one's political associations and beliefs is not absolute. It will yield to a subordinating interest of the state that is compelling in nature. *NAACP v. Alabama*, 357 U.S. 449, 464 (1958). Minnesota's securities laws constitute such a compelling interest. They have several interrelated purposes. One is to regulate the merits of securities offered for sale in the state. *State v. Investors Security Corp.*, 209 N.W.2d 405 (Minn. 1973). Another is to assure confidence in investments and trading. The laws are also designed to prevent deception. *Northwest Bancorp. v. Benson*, 6 F. Supp. 704 (D. Minn.), *aff'd*, 292 U.S. 606 (1934). Ever since the landmark Minnesota Supreme Court decision in *State v. Gopher Tire & Rubber Co.*, 146 Minn. 52, 117 N.W. 937 (1920), Minnesota securities laws have been broadly construed to protect Minnesota citizens from an endless variety of get-rich-quick schemes calculated to despoil credulous individuals of their savings.

The ALJ and the court below found that a compelling state interest had been shown. (App. C and F.) *See Local 1814 v. Waterfront Comm'n*, 667 F.2d 267 (2d Cir. 1981), and *Federal Election Comm'n v. The LaRouche Campaign*, 644 F. Supp. 120 (S.D.N.Y. 1986), *modified*, 817 F.2d 235 (2d Cir. 1987). In addition, the ALJ found that the Department had shown

that disclosure bore a substantial relation to the State's interest and balanced the Department's interest in disclosure against the likelihood of injury to the organizational Petitioners or their adherents if the desired information was released. (RA-24-26.) He found the Department's request satisfied each of these tests. *Id.*

The ALJ believed that he had a duty to approve only the least inclusive and narrowest inquiry necessary to accommodate the Department's interest, (RA-25). He pointed out that limited discovery had not worked in this case:

> Initially . . . the Respondents were ordered to disclose a limited number of names of individuals who loaned money to the Respondents. The Department argues that obtaining the names of Minnesota residents making loans to the Respondents in a piecemeal fashion is unworkable because the Respondent may produce the names of activists whose factual situations are least likely to fit the profile of an investor and who, it was implied, might be hostile toward him. Although the discovery originally ordered by the [ALJ] did not result in identifying any individuals in the same position as Mrs. Mitchell, the [ALJ] is not persuaded that a wholesale disclosure of all the contributors should be ordered at this time. Instead, disclosure options should be fashioned which identify persons like Mrs. Mitchell, rather than political activists who work for or who are members of the Respondent organization. The Respondents themselves have not made any suggestions on how that should be accomplished and have not indicated, even in general terms, the numbers of loans that may have been made by Minnesota residents.

(RA-25-26.) The ALJ then issued an order which included the following:

> Since the Commissioner is most directly concerned with the persons who have made loans evidenced by notes and who are not political activists; and since the privacy interests of those activists are more compelling than those of persons like Mrs. Mitchell, who are more concerned with a return on their investment, the [ALJ] believes that the following Order is appropriate:
>
> 1. That each organizational Respondent shall provide the Commissioner with a list of all the persons identified in Item 1, provided that no person must be disclosed who are officers, directors, employees, independent contractors, members or volunteer workers for the organizational Respondents, unless the required listing for any Respondent is less than 25 persons.
>
> 2. In the alternative, each Respondent shall provide the Judge, under seal, with a list of all the persons identified in Item 1 who, since September 1, 1983, made loans to them which are represented by a note or other promise of repayment by any Respondent (including all persons who purchased a note). The Judge shall then provide the Commissioner with the names of 30 persons from each list which are chosen at random (exclusive of the names already provided). Upon receipt of notice of the persons selected, the Respondents shall provide the Commissioner with the other information specified in Item 1.

(RA-26-27.)

The ALJ also issued a comprehensive protective order to protect the confidentiality of those persons whose names were

disclosed. (RA-28.) Despite the protective order, Petitioners refused to comply with the ALJ's order and did not provide the information which they were required to provide. After the Department renewed its complaint about Petitioners' noncompliance, the ALJ issued a new discovery order, modifying his previous order. This order accommodated Petitioners' desire to preserve the anonymity of their lenders to the maximum extent possible but required, at a minimum, that Petitioners provide the names and addresses to the ALJ who would then turn over 25 percent of the names to the Department. (RA-49.) This provision addressed the Department's legitimate concern that if Petitioners were allowed to choose the names they disclosed they would disclose the names of party activists who did not intend their loans as investments rather than persons such as Mrs. Mitchell who were solicited through boiler room tactics and who made their loans primarily as investments.

The ALJ also gave clear warning that sanctions would be imposed for noncompliance. When Petitioners refused to comply, the ALJ issued his order precluding Petitioners from contesting those portions of the Amended Cease and Desist Order to which the testimony of Petitioners' other Minnesota investors would have been directed if their identity had been disclosed.[6]

The ALJ's order was completely proper under the circumstances and does not constitute an abuse of discretion. The Department had every reason to believe that there were many

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[6] The paragraphs upon which preclusion was ordered, including the paragraph which contains the allegation that the notes were securities, are those specified in the Department's memorandum in opposition to a motion for a stay. Document No. 107 at p. 5. Petitioners never raised specific objections to any of these paragraphs.

other Minnesotans who have invested in the organizational Petitioners and who fit Mrs. Mitchell's profile. These persons were entitled to the protection of the Minnesota securities laws. The State had a compelling interest in learning their identity so that it could show that Mrs. Mitchell was not a "one shot phenomenon" but one of many victims of a boiler room operation designed to extract money from elderly and vulnerable persons.

CONCLUSION

For the foregoing reasons, the Petition For Writ of Certiorari should be denied.

Dated: November 14, 1988.

Respectfully submitted,

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RESPONDENT'S APPENDIX

	App.	Page
Amended Cease and Desist Order, Notice of Right to Hearing and Order Suspending Exemption dated July 17, 1986	A	RA-1
Prehearing Order dated August 7, 1986	B	RA-8
Discovery Order, Protective Order and Memorandum dated October 6, 1986	C	RA-13
Order Denying Motion to Dismiss Respondent Independent Democrats for LaRouche and Receiving Exhibits for Limited Purposes and Memorandum dated October 10, 1986	D	RA-29
Notice of Motion and Motion dated October 24, 1986 and Affidavit of Jerome L. Getz dated October 24, 1986	E	RA-40
Order Denying Motion for Preclusion, Establishing Reporting Requirements, and Setting a Hearing Date and Memorandum dated December 2, 1986	F	RA-44
Discovery Order dated December 15, 1986	G	RA-48
Order Denying Certification and a Stay dated January 13, 1987	H	RA-51
Order Imposing Sanctions for Noncompliance With Discovery and Memorandum dated January 27, 1987	I	RA-55

APPENDIX

APPENDIX A

STATE OF MINNESOTA
COMMISSIONER OF COMMERCE

OAH Docket No. COM/1-86-JL, 8-1005-689-2

In the Matter of CAUCUS DISTRIBUTORS, INC., and CAMPAIGNER PUBLICATIONS, INC., New York Corporations, INDEPENDENT DEMOCRATS FOR LaROUCHE, an unincorporated association, RON FREDMAN, RONALD R. BETTAG, PAUL GREENBERG, and all other persons and organizations acting in concert with the named respondents.

AMENDED CEASE AND DESIST ORDER, NOTICE OF RIGHT TO HEARING AND ORDER SUSPENDING EXEMPTION

TO: Caucus Distributors, Inc., Campaigner Publications, Inc. and Independent Democrats for LaRouche, 5th Floor, 304 W. 58th Street, New York, N.Y. 10019 and 4507 No. Kedzie Ave., Chicago, IL 60625.

Ron Fredman, Ronald R. Bettag, and Paul Greenberg, 4507 No. Kedzie Ave., Chicago, IL 60625.

And all other persons and organizations acting in concert with the named respondents.

Commissioner of Commerce Michael A. Hatch (hereinafter "Commissioner") has determined as follows:

1. On information and belief Respondents Caucus Distributors, Inc. ("CDI"), Campaigner Publications, Inc. ("CPI"), and Independent Democrats for LaRouche ("IDL") are all entities which are under the common control and direction of the National Caucus of Labor Committees ("NCLC"), an organization with its headquarters in Leesburg, VA. On information and belief, Respondents Ron Fredman and Ronald R. Bettag are officers or employees of Caucus Distributors, Inc. and Campaigner Publications, and Paul Greenberg is an authorized representative of Independent Democrats for LaRouche. Respondents Caucus Distributors, Inc., and Campaigner Publications, Inc., New York corporations, and Independent Democrats for LaRouche, an unincorporated association, acting jointly as part of a common cause and scheme through their officers, directors, agents, employees, assigns, affiliates, representatives and servants, including Respondents Ron Fredman, Ronald R. Bettag, and Paul Greenberg, have offered or sold promissory notes to persons in the State of Minnesota.

2. The promissory notes offered or sold by Respondents constitute securities within the meaning of Minn. Stat. § 80A.14, subd. 18 (1984).

3. These securities were not registered with the Commissioner prior to or at the time of their offer or sale in the State of Minnesota as required by Minn. Stat. § 80A.08 (1984), nor were said securities or their offer or sale exempt from the registration requirements of Minn. Stat. ch. 80A (1984), as amended.

4. Respondents are not licensed to sell securities in the State of Minnesota as required by Minn. Stat. § 80A.04 (1984), nor are they exempt from said licensing requirements.

5. Respondent Ron Fredman told a prospective purchaser of the promissory notes referred to in paragraph 2 that some banks were failing in order to convince her that it would be safer for her to invest her money with Respondent Caucus Distributors than to leave it in a bank, all of which constituted an act, practice or course of business which operates as a fraud or deceit upon a person in violation of Minn. Stat. § 80A.01, subd. (c) (1984).

6. Respondents have fraudulently misdated one of the promissory notes referred to in paragraph 2, all of which constituted an act, practice or course of business which operates as a fraud or deceit upon a person in violation of Minn. Stat. § 80A.01, subd. (c) (1984).

7. In connection with statements made during the offer and sale of the promissory notes referred to in paragraph 2, Respondents omitted to state material facts necessary in order to make the statements made not misleading, including:

a. That the primary source of money available to repay principal and interest on the notes was money obtained from other investors similarly situated;

b. That Respondent CDI was in default on its obligations to repay principal and interest to other investors and one or more judgments had been entered against Respondent CDI for failure to repay principal and interest when due;

c. That some of the promissory notes which would be issued in return for the funds invested in Respondent CDI might be issued by entities other than Respondent CDI;

d. Financial information from which the investors could determine the ability of Respondents to repay the notes when due; and

e. That Respondents were not licensed to sell securities in the State of Minnesota and that the promissory notes were not registered pursuant to the Minnesota securities laws, all in violation of Minn. Stat. § 80A.01, subd. (b) and (c) (1984).

8. On December 2, 1985, the Commissioner issued an Order for Written Statement, Production of Documents and Report of Sales, pursuant to Minn. Stat. § 80A.20 (1984), requiring that Caucus Distributors and Campaigner Publications furnish to the Commissioner within ten days, *inter alia*, a signed written statement, notarized and made under oath, setting forth all facts and circumstances concerning the offer or sale by Caucus Distributors and Campaigner Publications of promissory notes in the State of Minnesota during the period from November 1, 1982 to December 2, 1985 and to furnish copies of certain documents. Caucus Distributors and Campaigner Publications have failed to furnish to the Commissioner the specified written statement and all the documents requested.

9. Respondents, by the conduct described above, have violated the provisions of Minn. Stat. ch. 80A (1984), as amended, and should therefore be ordered to cease and desist from further violations thereof.

10. The following order is necessary and appropriate in the public interest or for the protection of investors and is consistent with the purposes fairly intended by the policy and provisions of Minn. Stat. ch. 80A (1984), as amended.

NOW, THEREFORE, IT IS HEREBY ORDERED, pursuant to Minn. Stat. § 80A.21 (1984), that Respondents shall cease and desist from offering or selling in the State of Minnesota the above-described or any other securities until com-

pliance with Minn. Stat. ch. 80A (1984), as amended, has been achieved and until further order of the Commissioner;

IT IS FURTHER ORDERED, pursuant to the provisions of Minn. Stat. § 80A.15, subd. 3 (1984), that any exemption from the registration requirements of Minn. Stat. ch. 80A (1984), as amended, claimed by or available to Respondents pursuant to the provisions of Minn. Stat. § 80A.15, subds. 1(g) and 2(a) (Supp. 1985) is hereby summarily suspended pending final determination of this Order;

IT IS FURTHER ORDERED, pursuant to Minn. Stat. § 80A.15, subd. 3 (1984) that Respondents shall show cause why the exemption contained in Minn. Stat. § 80A.15, subds. 1(g) and 2(a) (Supp. 1985) should not be revoked with respect to transactions by or on behalf of Respondents;

IT IS FURTHER ORDERED, pursuant to the provisions of Minn. Stat. § 80A.15, subd. 3 (1984) that Respondents shall appear at a hearing to be held at 9:00 a.m. on August 4, 1986, or at a later date if Respondents so request, in Courtroom 12 at the Office of Administrative Hearings, 4th Floor, Summit Bank Building, Minneapolis, Minnesota, before Administrative Law Judge Jon Lunde, 4th Floor, Summit Bank Building, Minneapolis, Minnesota 55415, telephone: (612) 341-7645 duly appointed in this matter by the Chief Administrative Law Judge of the State Office of Administrative Hearings.

The hearing in this matter will be held for the purpose of determining whether the summary suspension of exemption ordered herein and the Cease and Desist Order hereby issued shall be vacated or made permanent as provided by Minn. Stat. §§ 80A.15, subd. 3 and 80A.21 (1984). As provided by Minn. Stat. § 80A.15, subd. 4 (1984), the burden of proving an exemption or an exception from a definition is upon Re-

spondents. (An earlier hearing as to the Cease and Desist Order may be requested by Respondents, which will be held within seven days after the request for a hearing is received by the Commissioner. If no request is received, a hearing will be held as described above.)

The hearing will be conducted pursuant to the contested case procedures of the Minnesota Administrative Procedure Act, Minn. Stat. §§ 14.57-14.69 (1984), and pursuant to the rules of the State Office of Administrative Hearings, Minn. Rules pts. 1400.5100-1400.8400 (1985). Copies of these statutes and rules may be obtained from the Minnesota State Documents Center, 117 University Avenue, St. Paul, Minnesota 55155, telephone (612) 297-3000. A person requesting such copies must specify the statutes or rules requested. There is a charge for copies.

Respondents and the Department of Commerce (hereinafter "Department") will be parties to this proceeding. At the hearing, the Department will produce witnesses and documents to prove the allegations contained herein. Respondents may question the Department's witnesses. Respondents may then produce witnesses and documents to refute the Department's allegations. The Department may question Respondents' witnesses. Respondents and the Department will also be provided the opportunity to present arguments in support of their respective positions.

The parties must bring to the hearing all documents, records and witnesses they need to support their positions. Parties may obtain subpoenas to compel the attendance of witnesses or the production of documents, pursuant to Minn. Rules pt. 1400.7000 (1985). If data classified by law as nonpublic is admitted into evidence at the hearing, it may become public unless a party objects and obtains an order pursuant

to Minn. Stat. § 14.60, subd. 2 (1984) preserving the non-public status of the data.

All parties have the right to represent themselves or to be represented throughout these proceedings by an attorney or by a person of their choice, if not otherwise prohibited as the unauthorized practice of law.

If a party fails to attend or otherwise appear at the hearing in this matter after having been served with a copy of this Order, that party shall be deemed in default and the allegations or issues set forth herein may be deemed proved and the matter determined against the party without further proceedings.

Questions concerning the issues raised in this Order, informal disposition of this proceeding or discovery may be directed to Special Assistant Attorney General Jerome L. Getz, 1100 Bremer Tower, Seventh Place and Minnesota Street, St. Paul, Minnesota 55101, telephone (612) 296-9412.

A PARTY INTENDING TO APPEAR AT THE HEARING MUST FILE THE ENCLOSED NOTICE OF APPEARANCE WITH THE ABOVE-NAMED ADMINISTRATIVE LAW JUDGE WITHIN TWENTY (20) DAYS OF THE DATE OF SERVICE OF THIS ORDER.

Dated: July 17, 1986.

JAMES MILLER
Deputy Commissioner of
Commerce
State of Minnesota
500 Metro Square Building
St. Paul, Minnesota 55101
Telephone: (612) 296-2594

APPENDIX B

STATE OF MINNESOTA
OFFICE OF ADMINISTRATIVE HEARINGS

FOR THE MINNESOTA DEPARTMENT OF COMMERCE

COM/S-86-047-JL
8-1005-698-2

In the Matter of CAUCUS DISTRIBUTORS, INC., and CAMPAIGNER PUBLICATIONS, INC., New York Corporations, INDEPENDENT DEMOCRATS FOR LaROUCHE, an unincorporated association, RON FREDMAN, RONALD R. BETTAG, PAUL GREENBERG, and all other persons and organizations acting in concert with the named respondents.

PREHEARING ORDER

The above-entitled matter is pending before the undersigned Administrative Law Judge pursuant to a Cease and Desist Order, Notice of Right to Hearing and Order Suspending Exemption, filed on June 6, 1986, and an Amended Cease and Desist Order, Notice of Right to Hearing and Order Suspending Exemption filed on July 21, 1986.

Patrick J. Moran, Moran & Pilger, P.A., Attorneys at Law, 1221 Lamar, Suite 517, Houston, Texas 77010, has appeared on behalf of the above-named Respondents. Jerome L. Getz, Special Assistant Attorney General, 1100 Bremer Tower, 7th Place and Minnesota Street, St. Paul, Minnesota 55101, has

appeared on behalf of the Commissioner of Commerce (Commissioner).

Due to the unavailability of Respondents' counsel on the first hearing date ordered by the Commissioner, the hearing was rescheduled to commence on August 4, 1986, at the agreement of both counsel. The new hearing date was included in the Commissioner's Amended Cease and Desist Order. The Amended Order included additional charges and was followed by additional discovery requests from the Commissioner.

The hearing commenced at 9:00 a.m. on Monday, August 4, 1986. One witness testified at that time. Many of the witnesses subpoenaed by the Department failed to appear at that hearing, and the two who did, did not comply fully with subpoenas which had been mailed to them. Since it was obvious that a satisfactory record regarding the Respondent's activities could not be made without further discovery, and since there is a compelling state interest in the regulation of securities and a compelling need for further information in order to protect the public interest, the Administrative Law Judge ordered a continuance of the hearing and scheduled a prehearing conference, which was held at 10:00 a.m. the following day.

Based upon the discussions occurring at the prehearing conference, and the determinations made at that time, and upon all the files, records and proceedings herein,

IT IS HEREBY ORDERED:

1. On or before August 15, 1986, the Respondents shall file and serve their written objections to Exhibits 30 to 35 and indicate their willingness to stipulate to the admission of Exhibit 29. At the same time the Respondents shall file and serve a proposed protective order covering the information obtained by the Department during discovery. The Respon-

dents' filing must include a citation to the legal authorities relied upon. Within five calendar days after receipt of the Respondents' filing, the Commissioner shall file and serve his written response, which shall also contain a citation to relevant legal authority.

2. The Respondents shall, as agreed, immediately proceed to gather all the written records pertaining to any loans, whether paid or unpaid, made to any of the Respondents by Minnesota residents during the period from September 1, 1983 to April 30, 1986.

3. On or before August 27, 1986, the Respondents shall file and serve their objections to the disclosure of any information specified in paragraph 2 or give that information to the Commissioner. The objection must specify the information which it claims is protected by the First Amendment and contain a citation to the legal authorities relied upon. In addition, the objection shall be accompanied by argument and affidavits as to the injury to be suffered by the disclosure sought by the Commissioner, including the harassment or reprisal discovery may cause.

4. On September 5, 1986, the Commissioner shall file and serve his arguments for the disclosure of the information specified in paragraph 2 and his response to the arguments and authorities relied upon by the Respondents. The Commissioner's argument must state the precise information sought and the specific issues on which that information is relevant, and must state whether those issues are likely to be determinative. In addition, the Commissioner must state the reasons why his discovery request is the most restrictive means for accomplishing his objectives.

5. On September 5, 1986, the Respondent (Independent Democrats for LaRouche) shall file its Motion to dismiss the

charges against it based on its claim that the Commissioner's jurisdiction has been preempted by the Federal Elections Commission. At the same time, the Respondents shall file their arguments regarding the Commissioner's authority to subpoena nonresident Respondents and their officers, directors, employees or shareholders under Minn. Stat. § 80A.27, Subd. 8 (1984). The Commissioner shall respond to the Motion within the 10-day period specified in the rules of this Office and shall reply to the Respondents' arguments regarding subpoenas in the prehearing statement filed pursuant to paragraph 6.

6. On September 19, 1986, the Commissioner shall file a Prehearing Statement setting forth the law and the facts relied upon for its conclusion that the loans made to the Respondents by Minnesota residents and the notes issued by them for the repayment of those loans, if any, are securities. The Prehearing Statement shall also contain the Commissioner's arguments regarding the burden of proof in this proceeding, and must state the protective orders desired and any requests to close the hearing under Minn. Stat. § 14.60, Subd. 2, and the legal authority authorizing the actions requested. The Commissioner's Prehearing Statement shall be accompanied by any additional discovery requests or Motions deemed necessary to properly present his case. This is not intended to preclude earlier or later discovery requests or Motions, or limit the discovery undertaken of third persons.

7. On September 30, 1986, the Respondents shall file and serve their Prehearing Statement. It shall contain a brief summary of the law and facts relied upon by the Respondent supporting its argument that the loans and notes in issue in this proceeding are not securities and the exemptions, if any, it claims are applicable under Minn. Stat. § 80A.15. The Re-

spondent's prehearing statement shall also address their position on the burden of proof in this proceeding and their requests, if any, to close the hearing or seal any or all of the hearing record under Minn. Stat. § 14.60, Subd. 2. At the same time, the Respondent shall reply to any additional discovery requests the Department serves and files with its Prehearing Statement.

8. On Friday, October 3, 1986, a telephone conference will be held commencing at 3:00 p.m. The parties shall be available to discuss the status of this proceeding at that time and be prepared to discuss and resolve any discovery issues and other prehearing procedures that must be considered.

9. As suggested by Respondents and agreed to by the Commissioner, the hearing will resume on Wednesday, November 5, 1986, commencing at 9:00 a.m. The hearing will be held in Courtroom 12 at this Office and has been scheduled for completion within three days.

10. Noncompliance with any discovery orders or subpoenas issued by this Office will result in the imposition of sanctions pursuant to the rules of this Office, upon motion by an aggrieved party.

11. Any subpoenas requiring the attendance of nonresident Respondents or witnesses which are issued pursuant to Minn. Stat. § 80A.27, Subd. 8, shall be mailed at least 14 days prior to the commencement of the hearing and notice of the issuance of those subpoenas shall be simultaneously furnished to Respondents' counsel. Respondents' counsel shall be responsible for providing actual notice to his clients of the issuance of those subpoenas.

12. Pending further order, the Commissioner and his officers, employees and counsel shall not disclose or disseminate

any information gained through discovery other than is necessary to prepare and try this case.

Dated this 7th day of August, 1986.

JON L. LUNDE
Administrative Law Judge

APPENDIX C

STATE OF MINNESOTA
OFFICE OF ADMINISTRATIVE HEARINGS

FOR THE MINNESOTA DEPARTMENT
OF COMMERCE

COM/S-86-047-JL
8-1005-698-2

In the Matter of CAUCUS DISTRIBUTORS, INC., and CAMPAIGNER PUBLICATIONS, INC., New York Corporations, INDEPENDENT DEMOCRATS FOR LaROUCHE, an unincorporated association, RON FREDMAN, RONALD R. BETTAG, PAUL GREENBERG, and all other persons and organizations acting in concert with the named respondents.

DISCOVERY ORDER

The above-captioned matter is pending before the undersigned Administrative Law Judge pursuant to hearing Orders issued by the Commissioner of the Minnesota Department of Commerce. Patrick J. Moran, Moran & Pilger, P.A., Attorneys at Law, 1221 Lamar, Suite 517, Houston, Texas 77010, has

appeared on behalf of the above-named Respondents. Jerome L. Getz, Special Assistant Attorney General, 1100 Bremer Tower, 7th Place and Minnesota Street, St. Paul, Minnesota 55101, has appeared on behalf of the Commissioner.

Based upon the arguments and briefs of counsel and upon all the files, records and proceedings herein, and for the reasons set forth in the Memorandum accompanying this Order.

IT IS HEREBY ORDERED:

1. That each organizational Respondent shall forthwith provide the Commissioner with a list of all the persons identified in Item 1 who since September 1, 1983, made loans to them which are represented by a note, or other promise of repayment by any Respondent (including all persons who purchased a note), and the other information specified in Item 1, provided that no persons must be disclosed who are officers, directors, employees, independent contractors, members or volunteer workers for the organizational Respondents, unless the required listing for any Respondent is less than 25 persons.

2. In the alternative, each said Respondent shall forthwith provide the Judge, under seal, with a list of all the persons identified in Item 1 who, since September 1, 1983, made loans to them which are represented by a note, or other promise of repayment by any Respondent (including all persons who purchased a note). The Judge shall then provide the Commissioner with the names of 30 persons from each list which are chosen at random (exclusive the names already provided). Upon receipt of notice of the persons selected, the Respondents shall provide the Commissioner with the other information specified in Item 1.

3. The information specified in Item 2 shall be submitted to the Commissioner when the Respondents submit the in-

formation required under paragraph 1, or when notified of the random selection made by the Judge under paragraph 2.

4. That this Order is stayed for Independent Democrats for LaRouche until its Dismissal Motion on preemption grounds is decided.

5. That the information gained through discovery in this case is subject to the following PROTECTIVE ORDER:

a. That the Commissioner and his employees, investigators and counsel shall make no use of any information gained through discovery in this case other than such use as is necessary to prepare, try and decide the issues in this case. Any other disclosure, publication, or dissemination is prohibited in the absence of further order of the Administrative Law Judge or a court of law.

b. This Protective Order applies to all discovery previously obtained by the Commissioner and to any future information obtained through discovery which is claimed to be confidential under the First Amendment, and applies to any document in this proceeding which refers to or restates information gained through discovery.

c. The Commissioner shall retain all confidential information gained through discovery in a separate file that is not generally accessible except to his counsel and which is clearly identified as containing confidential data.

d. Before any confidential data is revealed to any person by the Commissioner's counsel, that person shall be advised of the terms of this Order.

e. The names of all persons who are given access to confidential data for the purposes set out in a. shall be entered on a log retained by the Commissioner's counsel.

f. When a final decision is reached in this case, all confidential information and copies thereof and a copy of

the Commissioner's log shall be returned to the party which produced them.

Dated this 6th day of October, 1986.

JON L. LUNDE
Administrative Law Judge

MEMORANDUM

In this proceeding, the Respondents have been charged with numerous violations of Minn. Stat. § 80A.01 *et seq.*, which govern the sale of securities in this state. Generally speaking, the Commissioner has alleged that the Respondents sold unregistered securities without a license and in connection with those sales acted in a fraudulent, deceptive or misleading manner. The Respondents have denied the charges made. In their view, the promissory notes they issued in return for loans made by Minnesota residents are not securities governed by the statutes, and even if they are, that they are exempt from registration.

In order to prepare for hearing, the Commissioner has requested an Order compelling the Respondents to provide the following information:

Item 1. The names and addresses of all persons residing in, or whose mailing addresses are located within the State of Minnesota to whom offers or sales of promissory notes or any other securities have been made; the dates of said offers or sales, the amounts thereof, the type or types of promissory notes or any other securities involved, if there are more than one, and the name of the person making such offer or sale. (Interrogatory No. 10).

Item 2. All writings of every kind and description, including handwritten notes, in the possession of Respondents

concerning loans by Minnesota residents to any of the Respondents during the period from September 1, 1983, to April 30, 1986. (Subpoena Request).

Item 3. The names of the shareholders of Campaigner Publications, Inc. (CPI). (Interrogatory No. 13).

The Respondents argue that the discovery sought by the Commissioner is protected under the First Amendment and that no order requiring disclosure should be issued. The Respondents' objections raise important issues which require careful consideration.

Freedom of association for the purpose of advancing ideas and airing grievances is protected from encroachment by the states under the First and Fourteenth Amendments. *Bates v. City of Little Rock*, 361 U.S. 516, 522-23 (1960). Since the compelled disclosure of a person's affiliation with groups engaged in the advocacy of ideas may have a chilling effect upon that person's freedom of association, the courts have recognized that a vital relationship exists between the freedom of association and privacy in one's associations. *NAACP v. State of Alabama*, 357 U.S. 449, 462 (1958). In that case the court stated that the inviolability of a person's privacy in group associations may be indispensable to the preservation of the freedom of association granted by the First Amendment, "particularly where a group espouses dissident beliefs." Hence, membership lists are entitled to protection under the First Amendment. *See also, Buckley v. Valeo*, 424 U.S. 1 (1975); *Pollard v. Roberts*, 283 F.Supp. 248 (E.D. Ark.), aff'd, 393 U.S. 14 (1968); *United States v. Citizen State Bank*, 612 F.2d 1091 (8th Cir. 1980). Under the First Amendment, the greatest solicitude must be paid to those threats aimed at suppressing an attempted exercise of political rights. *U.S. v. Carolene Products Co.*, 304 U.S. 144, 152-53, n.4 (1938).

The right to privacy in one's political associations and beliefs is not absolute. It will yield to a subordinating interest of the state that is compelling in nature. *NAACP v. Alabama*, 357 U.S. at 464. A significant encroachment on First Amendment rights cannot be justified by a mere showing of some legitimate governmental interests or a mere suspicion that a law has been violated. *Adolph Coors Co. v. Wallace*, 570 F.Supp. 202, 209 (N.D.Cal. 1983); *Buckley v. Valeo, supra*; *Pollard v. Roberts, supra*. For a state agency to require disclosure, in addition to establishing a compelling interest, the state must show that the disclosure sought bears a substantial relation to the state's interests and represents the least restrictive means for accomplishing the state's objectives. *NAACP v. Alabama*, 357 U.S. at 464; *Adolph Coors v. Wallace*, 570 F.Supp. at 208. It is also necessary to weigh the government's interest in disclosure against the likelihood of injury to an association or its members if the desired information is released. *Adolph Coors Co. v. Wallace*, 570 F.Supp. at 208. *See also, Matter of Agerter*, 353 N.W.2d 908, 913 (Minn. 1984).

The First Amendment rights discussed above apply when the state is seeking to subpoena information during the course of an investigation or when it seeks to obtain that information in the discovery process. *Adolph Coors Co. v. Wallace, supra*; *Marrese v. American Academy of Orthopaedic Surgeons*, 706 F.2d 1488 (7th Cir. 1983); *Savola v. Webster*, 644 F.2d 743 (8th Cir. 1981).

State's Interest in Obtaining Disclosure

The state's securities laws have several interrelated purposes. One is to regulate the merits of securities offered for sale in the state. *State v. Investors Security Corporation*, 209 N.W.2d 405 (Minn. 1973). Another is to assure confidence in

investments and trading. The laws are also designed to prevent deception and save credulity and ignorance from imposition. *Northwest Bancorporation v. Benson*, 6 F.Supp. 704 (D. Minn. 1934), aff'd. 292 U.S. 606. Hence, the securities laws of this state have been broadly construed to protect Minnesota citizens from an endless variety of get-rich-quick schemes calculated to despoil credulous individuals of their savings. *State v. Gopher Tire & Rubber Co.*, 146 Minn. 52, 177 N.W. 937 (1920).

In *Local 1814 v. Waterfront Commission of New York Harbor*, 667 F.2d 267 (2nd Cir. 1981), the court found that the Waterfront Commission investigating accusations that certain members of a union had been coerced into making donations to the union's Political Action Committee had a compelling interest in obtaining the names of employees who had recently authorized such payroll deductions from their employers. The compelling interest being its interest in fighting crime on the waterfront and preventing the extraction of money by coercive means. The state's interest in regulating securities is no less compelling than the Commission's interest in that case. Since the state has a compelling interest in regulating securities, it must be determined whether the precise materials sought in this case are relevant to the charges made. If they are, the rights and interests of the parties must be balanced to determine whether the public interest overrides the First Amendment rights of the Respondents and others, and whether the discovery request is framed in the least inclusive and intrusive manner possible. *Adolph Coors Co. v. Wallace*, 570 F.2d at 208. *Cf. Savola v. Webster*, 644 F.2d at 746-747.

Relevancy

When First Amendment rights are asserted, the state's interest in disclosure will be relatively weak unless the informa-

tion it seeks to obtain goes to the heart of the matter or is crucial to the case. *Adolph Coors Co. v. Wallace*, 570 F.2d at 208. In such cases the state must demonstrate a high degree of relevancy of the information sought. Official curiosity is insufficient. *Id.* Thus, in *Pollard v. Roberts*, 283 F.Supp. at 57, the court refused to require the Republican Party to disclose the identities of party contributors and the amounts of their contributions in connection with an investigation of suspected vote buying by a state prosecuting attorney. The court found that the identity of party contributors was not reasonably relevant to the state's investigation and concluded that the disclosure of the information was not sufficiently cogent and compelling to outweigh the legitimate and constitutionally protected interests of the Republican party and its contributors in having that information remain private.

In this case, the state has alleged that Respondents have failed to register unexempt securities they sold in this state, thereby violating Minnesota Law. In addition, it has alleged that the sales were made by persons having no license to sell securities, contrary to the state securities laws, and that various fraudulent, misleading or untruthful acts or omissions were made by the Respondents in connection with the sales that were made. The Respondents' position is that the notes they issued are not securities, or if they are, they are exempted from the provisions of Chapter 80A as commercial paper arising out of current transactions or as isolated sales for purposes of Minn. Stat. § 80A.15, subd. 1(g) and subd. 2(a). There are no Minnesota cases which have discussed the circumstances when a note is not a security for purposes of Minn. Stat. § 80A.14, subd. 18. However, other courts have considered the issue. They have usually adopted a commercial-investment test or a risk-capital test to make that determina-

tion. Those tests require a consideration of a number of factors, including:

1. Whether the transaction involved consumer financing.
2. Whether the note is secured by a mortgage on a home.
3. Whether the note is a short-term note secured by a lien on small business.
4. How a reasonable businessman in the commercial world would characterize the instrument.
5. The use to which the proceeds of the note are put.
6. Whether profits come from the efforts of others.
7. The number of notes issued, the number of payees to whom they were issued, and the dollar amounts of the transactions.
8. Whether they are demand notes or other long-term notes.
9. How the parties characterize the notes.
10. How the notes were marketed or characterized by the persons issuing them.
11. Whether the person making the loan is within the class of persons the Legislature was trying to protect under the law.
12. The investors who were solicited by the issuers of the notes.
13. Whether the investor has contributed risk capital subject to the entrepreneurial or managerial efforts of the seller or issuer.
14. The existence and extent of collateralization.

In Item 1, the Commissioner seeks to obtain the names and addresses of all persons in Minnesota who were offered or sold promissory notes or other securities by the Respondents, the dates of the offers or sales, the amounts, and the types of promissory notes or other securities involved, and the name

of the person making the offer or sale. That Interrogatory goes to the heart of this case and the isolated sales exemption claimed by the Respondents. In order to determine if the notes are securities and if that exemption is applicable, the Department must, at a minimum, know how many securities (notes) were issued or sold to Minnesota residents and whether those notes were commercial in nature or involved an investment, using the criteria set forth above.

Prior to August 1, 1985, the isolated sales of securities were excluded from the statutory registration requirements under section 80A.15, subd. 2(a). The exemption applied only if no more than five securities were sold during any period of 12 consecutive months,[1] and where the sales were made by the issuer, the exemption applied only if the issuer reasonably believed that all buyers were purchasing the securities for investment and the securities were not advertised for sale to the general public or through a program of general solicitation by various means including mail or telephone. Since the Respondent is claiming that the sales it made, if any, were isolated sales, it will be necessary to determine the number of sales that were made during any period of 12 consecutive months, whether the sellers reasonably believed that all buyers were purchasing for investment (rather than resale) and whether the securities sold were advertised for sale to the general public or through a program of general solicitation by means of mail or telephone. Moreover, the circumstances surrounding the sale or issuance of each note must be considered to determine if it is a security. All these factors are highly relevant. Indeed, information regarding them is crucial to the state's case. Therefore, the Judge is persuaded that the

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[1] After August 1, 1985, the statute was amended to permit no more than ten isolated sales.

Department has demonstrated a compelling need to obtain the names and addresses of those persons in Minnesota to whom notes or other securities have been sold since August 31, 1983. Likewise, during the same period of time, the Department must be able to obtain the business records, notes and correspondence in the Respondents' possession which pertain to those loans.

Injury Caused by the Discovery Requested

The Respondents have argued that their First Amendment rights, as well as the rights of their members and contributors, will be substantially burdened by the disclosures sought by the Department. When a party claims that it will suffer injury due to the compelled disclosure of membership information or the identities of its "contributors", its claims must be carefully scrutinized to determine whether disclosure will have a chilling affect on the freedom of association. The party objecting to discovery on First Amendment grounds is not required to establish a "chill" with certainty, but need only show some probability that harassment might follow from the disclosure. *Adolph Coors Co. v. Wallace, supra* at 208, n. 18, and 209-10. Thus, in *Buckley v. Valeo, supra,* the United States Supreme Court said that unduly strict requirements of proof of potential harassment could impose a heavy burden on small organizations and they must be allowed sufficient flexibility in proving an injury. In this case, Respondents have shown that Lyndon LaRouche and his followers have been the subject of a substantial amount of criticism and adverse publicity from the Democratic Party. Respondents have not submitted Affidavits showing the experiences of their members or contributors in professional and social setting when their association has become known, and there is little evidence of specific incidents of past or present harassment of members

or contributors resulting from their associational ties. However, a serious claim of infringement has been made. The persons who have made loans to the Respondents will undoubtedly be contacted by departmental investigators or its counsel, and those persons may be summoned to depositions or to the hearing. This could breed apprehension in the minds of those contributors that their support of the Respondents will be the subject of public inquiry, investigation and litigation. As a result, they may cease to provide financial assistance, and if their experience becomes known, others may choose not to provide financial assistance or support to the Respondents. Moreover, the policies of the LaRouche organizations are not popular ones and the disclosure of the identities of their supporters could have an effect on the supporters future employment or appointment to public office. Therefore, the Judge is persuaded that the claims of a chilling effect are sufficient to require that the Department establish a compelling need to obtain the information sought.

Balance of Interests.

Although the First Amendment privacy rights of the Respondent organizations and their members and supporters may be burdened by the disclosure sought, the state's interest in obtaining disclosure outweighs those privacy interests. If the state cannot obtain the requested information, its ability to regulate the securities of political associations generally will be severely crippled if not destroyed, and in this case, it is likely that the charges will have to be dismissed. Therefore, it is concluded that the state's interests outweigh those asserted by the Respondents. Although there is some reason to question the extent to which the political representations of any group should be reviewed for accuracy, it has not been argued that political associations are exempt from the secu-

rities act, and the only decision bearing on that issue suggests that no such exemption exists. *Cf. SEC v. World Radio Mission, Inc.*, 544 F.2d 535 (1st Cir. 1976). The information sought goes to the essence of the charges in this case and must be disclosed if the state is to carry out its statutory responsibilities. Moreover, the states action is not based on a mere suspicion of impropriety or official curiosity. On the contrary, it is based on a bona fide complaint. Therefore, it is concluded that the interests of the state outweigh those asserted by Respondents. This is most true as to those persons who have made loans to the Respondent primarily as an investment or for profit motives, but is less true for members and supporters of the principles espoused by Lyndon LaRouche whose loans may have been made primarily for political purposes. Nonetheless, the states interests, in balance, also outweigh those of the latter group.

Least Inclusive and Intrusive Discovery

When the state has a compelling interest in obtaining discovery of information that is protected under the First Amendment, the only discovery authorized is the least inclusive and narrowest inquiry necessary to accommodate that interest. *Adolph Coors Co. v. Wallace, supra,* and *Savola v. Webster, supra.* Moreover, it has been suggested that discovery proceed in stages, where possible, to avoid unnecessary disclosures. *Marrese v. American Academy of Orthopaedic Surgeons, supra.* Thus in *Local 1814 v. The Waterfront of Commission of New York Harbor, supra,* the court modified the Waterfront Commission subpoena of the names of all longshoremen who had recently authorized payroll deductions to a union's Political Action Committee to permit only a ten percent random sampling. Initially, a similar approach was taken by the Judge in this case and the Respondents were

ordered to disclose a limited number of names of individuals who loaned money to the Respondents. The Department argues that obtaining the names of Minnesota residents making loans to the Respondents in a piecemeal fashion is unworkable because the Respondent may produce the names of activists whose factual situations are least likely to fit the profile of an investor and who, it was implied, might be hostile toward him. Although the discovery originally ordered by the Judge did not result in identifying any individuals in the same position as Mrs. Mitchell, the Judge is not persuaded that a wholesale disclosure of all the contributors should be ordered at this time. Instead, disclosure options should be fashioned which identify persons like Mrs. Mitchell, rather than political activists who work for or who are members of the Respondent organizations. The Respondents themselves have not made any suggestions on how that should be accomplished and have not indicated, even in general terms, the numbers of loans that may have been made by Minnesota residents.

Since the Commissioner is most directly concerned with the persons who have made loans evidenced by notes and who are not political activists; and since the privacy interests of those activists are more compelling than those of persons like Mrs. Mitchell, who are more concerned with a return on their investment, the Judge believes that the following Order is appropriate:

1. That each organizational Respondent shall provide the Commissioner with a list of all the persons identified in Item 1 who, since September 1, 1983, made loans to them which are represented by a note, or other promise of repayment by any Respondent (including all persons who purchased a note) and the other information speci-

fied in Item 1, provided that no persons must be disclosed who are officers, directors, employees, independent contractors, members or volunteer workers for the organizational Respondents, unless the required listing for any Respondent is less than 25 persons.

2. In the alternative, each Respondent shall provide the Judge, under seal, with a list of all the persons identified in Item 1 who, since September 1, 1983, made loans to them which are represented by a note or other promise of repayment by any Respondent (including all persons who purchased a note). The Judge shall then provide the Commissioner with the names of 30 persons from each list which are chosen at random (exclusive the names already provided). Upon receipt of notice of the persons selected, the Respondents shall provide the Commissioner with the other information specified in Item 1.
3. The information specified in Item 2 shall be submitted to the Commissioner when the Respondents submit the information supplied under paragraph 1, or when notified of the random selection made by the Judge under paragraph 2.

The Respondents CPI shall not be required to disclose the names of its shareholders at this time. Although the Department has argued that all the Respondent organizations are under common control such that the notes they have issued should be aggregated for purposes of determining whether or not the statutory minimum number of sales was exceeded at any time, it will not be necessary to disclose those names unless it later appears that no violation existed apart from aggregation.

Protective Order

Under the Rules of Civil Procedure for District Courts, Rule 26.03, an order may be issued to protect a person or party from annoyance, embarrassment, or oppression, which might follow from the disclosure of information. Those rules may be applied in administrative proceedings under Minn. Rule 1400.6600 (1985) and Minn. Stat. 14.60, subd. 2 (1984). The privacy interests of a party include the privacy of their political associations, and is a proper subject of a Protective Order under the civil rule and the statute cited above. *Settle Times Co. v. Rhinehart*, 104 S.Ct. 2199, 2208, n.21, 81 L.Ed.2d 17 (1986). Based on the holding in that case and the discussion in this Memorandum, it is concluded that a Protective Order must be issued in this case to avoid dissemination or publication of the identities of persons who have made loans to the Respondents and the identities of persons who are employees, workers, activists, founders, directors, or owners of the Respondent organizations. The Protective Order should cover all information gained by the Complainant through the discovery process and may be modified only upon further order.

J.L.L.

APPENDIX D

STATE OF MINNESOTA
OFFICE OF ADMINISTRATIVE HEARINGS

FOR THE MINNESOTA DEPARTMENT OF COMMERCE

COM/S-86-047-JL
8-1005-698-2

In the Matter of CAUCUS DISTRIBUTORS, INC., and CAMPAIGNER PUBLICATIONS, INC., New York Corporations, INDEPENDENT DEMOCRATS FOR LaROUCHE, an unincorporated association, RON FREDMAN, RONALD R. BETTAG, PAUL GREENBERG, and all other persons and organizations acting in concert with the named respondents.

ORDER DENYING MOTION TO DISMISS RESPONDENT INDEPENDENT DEMOCRATS FOR LAROUCHE AND RECEIVING EXHIBITS FOR LIMITED PURPOSES

The above-captioned matter is pending before the undersigned Administrative Law Judge pursuant to hearing Orders issued by the Commissioner of the Minnesota Department of Commerce (Commissioner). Patrick J. Moran, Moran & Pilger, P.A., Attorneys at Law, 1221 Lamar, Suite 517, Houston, Texas 77010, has appeared on behalf of the above-named Respondents. Jerome L. Getz, Special Assistant Attorney General, 1100 Bremer Tower, 7th Place and Minnesota Street,

St. Paul, Minnesota 55101, has appeared on behalf of the Department of Commerce (Department or State).

Based upon the arguments and briefs of counsel and upon all the files, records and proceedings herein, and for the reasons set forth in the Memorandum accompanying this Order,

IT IS HEREBY ORDERED: That the Dismissal Motion on preemption grounds filed by Independent Democrats for LaRouche be and it hereby is denied; and Exhibits 30-35 are received in evidence for the purposes stated in the attached Memorandum.

Dated this 10th day of October, 1986.

JON L. LUNDE
Administrative Law Judge

MEMORANDUM

The Respondent, Independent Democrats for LaRouche (IDL), argues that it must be dismissed from this proceeding because the Department's jurisdiction to regulate it has been preempted by the Federal Election Campaign Act Amendments of 1974, amending 2 U.S.C. § 431 *et seq.* IDL bases its preemption argument on the provisions in section 453, which reads as follows:

> The provisions of this Act, and of rules prescribed under this Act, supercede and preempt any provision of State law with respect to election to Federal office.

Federal law is supreme and prevails over conflicting state laws, which are subordinate. In determining whether a federal statute supersedes state laws, or whether federal laws have occupied a field in such a way as to exclude state regulation, the entire scheme of the federal statute must be considered, including the nature of the power exerted and the object sought to be obtained. *See, generally,* 81A C.J.S. § 24b, p. 329.

Federal law will preempt state law when (1) Congress expresses a clear intent to preempt, (2) there is a conflict between state and federal law, (3) compliance with both state and federal laws is physically impossible, (4) there is an implicit barrier to state regulation in a federal law, (5) federal legislation is comprehensive and occupies an entire field leaving no room for state supplementation, or (6) state law creates an obstacle to the accomplishment and execution of Congressional objectives. *Louisiana Public Service Commission v. FCC*, —— U.S. ——, 106 S.Ct. 1890, 1898-99 (1986).

IDL argues that Congress clearly intended to occupy the field with respect to loans and other contributions to candidates for federal office and to preempt state securities law applicable to such loans, and it argues that state securities laws create an irreconcilable conflict with federal laws which requires that they be preempted. Those arguments are not persuasive. Congress did not intend to occupy the field of the regulation of loans or other campaign contributions received by campaign committees. This conclusion is supported by the language of section 453, the legislative history of the federal laws, court decisions, and interpretations of the Federal Elections Commission (FEC).

Section 453, cited above, states that the federal laws preempt state law "with respect to election to federal office." The state's securities laws are not "election laws" and they do not specifically deal with loans or contributions received by campaign committees working for a person's election to federal office. Nowhere in the 1984 federal laws or in anything cited by the Respondent is there language or authority which suggest that Congress intended to preempt laws of general application outside the area of elections. Moreover, even the preemption mandated in the federal law is not complete as to

election laws. Such being the case, it is unlikely that Congress intended to preempt laws of general application outside the area of elections. The purpose of the 1984 federal law[1] is expressed as follows:

> To impose overall limitations on campaign expenditures and political contributions; to provide that each candidate for Federal office shall designate a principal campaign committee, to provide for a single reporting responsibility with respect to receipts and expenditures by certain political committees; to change the time for the filing of reports regarding campaign expenditures and political contributions; to provide for public financing of Presidential nominating conventions and Presidential primary elections; and for other purposes.

The express preemption in section 453 applies only to laws dealing with the election to federal office. Moreover, even in that area, the Federal Act was not intended to preempt state laws relating to the manner of qualifying as a candidate or the dates and places of elections. *See*, Senate Conf. Report No. 1237, reprinted at 1974 U.S. Code Cong. & Ad. News 5587, 5618, 5668.

Courts that have considered the scope of the Federal Act have found that state laws pertaining to elections are not necessarily preempted by the Federal Act. In *Pollard v. Board of Police Commissioners*, 665 S.W.2d 333 (Mo.banc. 1984), *cert. den.*, 105 S.Ct. 3534, the Missouri Supreme Court concluded that the Act did not preempt a state statute prohibiting officers or employees of the Kansas City Police Department from making political campaign contributions in any elections. In that case, the court noted that the legislative history

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[1] Pub.L. No. 93-433, 88 Stat. 1263-1304 (codified as amended at 2 U.S.C., §§ 431-55 (1976)).

of the Federal Act clearly shows that Congress did not intend to preempt state little Hatch Acts or other similar laws. It concluded that the legislative history makes it clear that the statute was intended to preempt the limited field of statutes imposing restrictions on candidates for federal office and their campaign committees. *Id.* at 337. Likewise, in *Reeder v. Kansas City Bd. of Police Com'rs.*, 733 F.2d 543 (8th Cir. 1984), the court reviewed the same Missouri statute and concluded, as did the Missouri Supreme Court, that the Missouri law prohibiting campaign contributions by officers or employees of the Kansas City Police Department was not preempted by the Federal Act.

In *Friends of Phil Gramm v. Americans for Phil Gramm*, 587 F.Supp. 769 (E.D.Va. 1984), the court found that the Federal Election Act preempts state law within the scope of the Federal Act's prohibition against political committees including the name of any candidate in its title if it is not an authorized committee. However, in addressing the issue of state laws pertaining to fraud, the court stated (p. 776):

> The right to use a candidate's name described above is not unqualified. The First Amendment does not protect knowingly false statements. * * * Nor does the Federal Election Act categorically preclude a state law cause of action for fraud. The Act nowhere specifically addresses the problem of fraud and political advertising. Congress obviously did not intend completely to preclude state regulation in this area, thus giving political organizations license to mislead. The only reasonable conclusion is that Congress intended to leave regulation of fraud in political advertising to the states, except where such regulation conflicts with the Act's specific provisions.

Similarly, in *Washington Education Ass'n v. Smith*, 96 Wash. 2d 601, 638 P.2d 77 (1981), the Washington Supreme Court found that a state statute that did not permit the state budget director to allow voluntary payroll deductions for employees for purposes of making direct contributions to political action committees of the employees' labor associations was not in conflict with the Federal Election Campaign Act and was not preempted by it, because there was nothing in the Federal Act that required employers to establish payroll deduction plans for its employees.

Advisory opinions issued by the FEC also indicate that the Federal Act does not generally preempt state law. Thus, in AO 1980—47, CCH Federal Election Campaign Financing Guide, ¶ 5497, the FEC issued an advisory opinion stating that the Federal Act does not preempt a Maryland law prohibiting payments to certain workers on an election day. Likewise, in an advisory opinion dated October 27, 1976, the FEC stated that a gross receipts tax on concert tickets for admission to live entertainment provided in connection with a fundraiser of a political committee was a revenue measure and not an election matter preempted by the Federal Act. CCH Federal Election Campaign Financing Guide, ¶ 6043.

The cases and opinions cited above persuade the Judge that the federal laws relied upon by the Respondent IDL do not express an intent to preempt all state laws which may affect campaign committees, or occupy the field of regulation of such committees. Therefore, a finding of preemption is appropriate only if there is a conflict between the state's securities law and the federal law, if compliance with both is physically impossible or if state law creates an obstacle to the accomplishment and execution of Congressional objectives. IDL has not shown that any of those factors exist here and the Judge is

persuaded by the Department's arguments that none of the factors set out in *Louisiana Public Service Commission v. FCC, supra,* apply.

Under 2 U.S.C. § 431(8)(A), only loans made for the purpose of influencing election to federal office are covered by the Federal Act. Loans made for investment purposes do not appear to come within the statute, and IDL has presented no evidence that the loans made to it by Minnesota residents were made to influence election to Federal office. Even if some, or all of the loans made to IDL were made, in whole or in part, to influence election to Federal Office, IDL has not shown that state regulation of such loans, when evidenced by notes or other securities, are preempted. The Federal Act does not occupy the field, and IDL has not shown that the state's regulation of loans evidenced by notes or other securities is inconsistent with any specific statutory provision or that state regulation of loans involving securities frustrates any federal purpose.

As noted in the Department's brief, preemption should not be found unless an intent to preempt is the clear and manifest purpose of Congress and, where possible, the historic police powers of the state should be reconciled with federal acts. In this case, the Judge is persuaded that state securities laws have not been totally preempted by the federal act, and since no specific inconsistencies have been shown, the Judge is persuaded that the state laws applicable to the securities issued by IDL have not been preempted in whole or in part.

IDL also argued that the security acts are preempted under 18 U.S.C., §§ 594-607. However, the legislative history cited by the parties clearly shows that Congress intended to preempt state laws relating to the specific crimes mentioned, and did not intended to affect the states powers to prohibit false

registration, voting fraud, theft of ballots and similar offenses under state law. IDL has cited no authority to indicate that there is any conflict between state law and the criminal laws cited above, that those criminal laws were designed to preempt state securities regulations, or that any inherent inconsistency exists. For all these reasons it is concluded that the state's authority to regulate IDL, assuming it is an authorized political committee for purposes of the federal statutes, has not been preempted.

Admissibility of Exhibits 30-35.

The Commissioner has offered into evidence certified copies of the pleadings, orders and subpoenas issued by the securities departments of other states. Included in the pleadings and orders issued are copies of affidavits made by individuals in those states regarding loans made to the Respondents, and copies of checks and notes pertaining to those loans.

The exhibits have been offered to show (1) that a number of securities commissioners around the country have concluded that analogous loans are securities under the laws of their states, (2) that the Respondents have solicited investments in other states which, if they had taken place in Minnesota, would be in violation of Minnesota law, and (3) that the transaction with Mrs. Mitchell was not an isolated phenomenon, i.e., that the Respondents have offered or sold notes or made loans in other states. Respondents object to the admissibility of the exhibits on hearsay grounds. The Commissioner argues, however, that they are admissible under Rule 803(8) as public records. Rule 803(8) of the Minnesota Rules of Evidence provides:

> (8) Public records and reports. Records, reports, statements, or data compilations, in any form, of public offices or agencies, setting forth (A) the activities of the office

> or agency, or (B) matters observed pursuant to duty imposed by law as to which matters there was a duty to report, excluding, however, in criminal cases and petty misdemeanors matters observed by police officers and other law enforcement personnel, or (C) in civil actions and proceedings except petty misdemeanors and against the State in criminal cases and petty misdemeanors, factual findings resulting from an investigation made pursuant to authority granted by law, unless the sources of information or other circumstances indicate lack of trustworthiness.

Under Exception (A), records maintained by a state agency are admissible to prove the truth of the matters contained in them. This exception applies, for example, to records of receipts and disbursements and licenses issued. The allegations in complaints and orders of any agency are not admissible under this exception. Likewise, those allegations are not admissible as matters observed, because they were not, or as investigative reports. In *U.S. v. Stone*, 604 F.2d 922, 924-26 (5th Cir. 1979), the exception for investigative reports was held to exclude reports pertaining to specific litigation. Therefore, the complaints and orders issued by other state agencies are inadmissible to prove the truth of the matters asserted in them. Nonetheless, they will be received in evidence for the limited purpose of showing that a particular complaint or order was issued. For such a purpose, they are not hearsay evidence.

The affidavits contained in the records of other state agencies, including copies of notes and checks evidencing loans made to the Respondents are also inadmissible under Rule 803(8) to prove the truth of the matters asserted in them. However, that does not end the inquiry that must be made.

The rules of evidence in administrative proceedings are governed by Minn. Stat. § 14.60, subd. 1, which reads:

> Subd. 1. Admissibility. In contested cases agencies may admit and give probative effect to evidence which possesses probative value commonly accepted by reasonably prudent persons in the conduct of their affairs. * * *

Under the statute, as set forth in Minn. Rule 1400.7300, subp. 1 (1985) hearsay evidence on which reasonable prudent persons are accustomed to rely in the conduct of their serious affairs is admissible.[2] In determining whether hearsay evidence is admissible under this rule, McCormick has suggested several criteria that should be considered: (1) the nature of the evidence, (2) whether better evidence available, (3) how precise the agency's factfinding must be, and (4) the administrative policy behind the statute being enforced, i.e., is this a high volume, low cost proceeding where an expeditious decision is needed. McCormick, Evidence, § 353, p. 1013-1016 (3d.ed. 1984).

Based on these factors, it is concluded that the affidavits and supporting documentation in the disputed exhibits may be admitted into evidence for the limited purpose of showing that persons in other states have made loans to the Respondents which are represented by promissory notes. That evidence has a sufficient degree of reliability to be admitted because it reflects transactions with more than one individual in more than one state and was no doubt investigated by each state agency before formal action was taken. The investigations that necessarily occurred, followed as they were by formal action, tend to support the reliability of those docu-

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[2] Affidavits are generally inadmissible in civil proceedings but are sometimes admissible in administrative proceedings. 2A C.J.S., Affidavits, § 58, p. 505-06.

ments. Similar policy reasons permit investigatory reports to be admitted in evidence under Rule 803(8). Moreover, it is not practical to obtain better evidence regarding the Respondent loans in other states. The primary inquiry in this case involves the Respondent's activities in this state, but in determining whether the Respondents have sold securities, it is appropriate to consider whether loans were made in other states, even though it is not necessary or desirable to consider the specifics of those transactions. Hence, the affidavits and other supporting documentation in the exhibits will be received for the limited purpose of showing that loans were made to the Respondents in other states. However, they will not be received for the purpose of showing that those loans were securities.

J.L.L.

APPENDIX E

STATE OF MINNESOTA
OFFICE OF ADMINISTRATIVE HEARINGS
FOR THE
DEPARTMENT OF COMMERCE

OAH Docket No. COM/1-86-047-JL
8-1005-698-2

In the Matter of CAUCUS DISTRIBUTORS, INC., and CAMPAIGNER PUBLICATIONS, INC., New York Corporations, INDEPENDENT DEMOCRATS FOR LaROUCHE, an unincorporated association, RON FREDMAN, RONALD R. BETTAG, PAUL GREENBERG, and all other persons and organizations acting in concert with the named respondents.

NOTICE OF MOTION AND MOTION

TO: EACH OF THE ABOVE-NAMED RESPONDENTS.

PLEASE TAKE NOTICE that pursuant to the Rules of the Office of Administrative Hearings of the State of Minnesota, Minn. Rules 1400.6600 and 1400.6700, the Enforcement Division of the Minnesota Department of Commerce has submitted the motion below to the Honorable Jon Lunde, Administrative Law Judge. The motion is based on the affidavit of Jerome L. Getz, sworn to on October 24, 1986 and all the files herein. Please be advised that if you wish to contest the motion, you must file a written response with the judge and serve copies on all parties within ten (10) working days after

it is received. A telephone hearing will be conducted at 10:00 a.m. on October 28, 1986.

Pursuant to Minn. Rules 1400.6700, subp. 3 petitioner hereby applies for an order of the Judge precluding Respondents from contesting the allegations in the Amended Cease and Desist Order or raising any affirmative defenses to the allegations. In the alternative, Petitioner seeks an order of the Judge that all allegations in the Amended Cease and Desist Order which Petitioner might be able to prove through the testimony of the persons whose names were to be disclosed pursuant to paragraphs 1 and 2 of the Administrative Law Judge's discovery order dated October 6, 1986 be deemed admitted and that Respondents be precluded from raising any affirmative defenses which might be rebutted by the testimony of such persons.

Dated: October 24, 1986.

HUBERT H. HUMPHREY, III
Attorney General
State of Minnesota
By: JEROME L. GETZ
Special Assistant
Attorney General
1100 Bremer Tower
7th and Minnesota Street
St. Paul, Minnesota 55101
Telephone: (612) 296-9412
Attorneys for Petitioner

STATE OF MINNESOTA
OFFICE OF ADMINISTRATIVE HEARINGS
FOR THE
DEPARTMENT OF COMMERCE

OAH Docket No. COM/1-86-047-JL
8-1005-698-2

In the Matter of CAUCUS DISTRIBUTORS, INC., and CAMPAIGNER PUBLICATIONS, INC., New York Corporations, INDEPENDENT DEMOCRATS FOR LaROUCHE, an unincorporated association, RON FREDMAN, RONALD R. BETTAG, PAUL GREENBERG, and all other persons and organizations acting in concert with the named respondents.

AFFIDAVIT OF JEROME L. GETZ

STATE OF MINNESOTA
COUNTY OF RAMSEY—ss.

JEROME L. GETZ, being sworn, says:

1. I am a Special Assistant Attorney General of the State of Minnesota and am attorney for petitioner herein. I make this affidavit in support of petitioner's motion for an order seeking relief from respondents for failure to comply with a discovery order previously issued herein by the Administrative Law Judge.

2. On October 6, 1986 the Administrative Law Judge issued a discovery order in which he required each organizational respondent to provide petitioner "forthwith" with a list of all persons residing in, or whose mailing address is located within the State of Minnesota to whom offers for sales

of promissory notes or any other securities have been made, the dates of said offers of sales, the amounts thereof, the type or types of promissory notes or any other securities involved, if there are more than one, and the name of the person making such offer or sale, provided that no persons must be disclosed who are officers, directors, employees, independent contractors, members or volunteer workers for the organizational respondents, unless the required listing for any respondent is less than 25 persons. In the alternative, the Administrative Law Judge ordered each organizational respondent to provide the Judge "forthwith", under seal, with a list of all such persons who since September 1, 1983, made loans to them which are represented by a note, or other promise of repayment by any respondent (including all persons who purchased a note).

3. Seventeen days have now passed since the Judge's order was issued and Respondents have not provided Petitioner with any names as required under the discovery order.

4. The hearing in this proceeding is scheduled to resume on November 5. Petitioner cannot properly prepare to present its case without the disclosure of the information called for under the discovery order. Because it will take time to locate and interview these persons, Petitioner is already prejudiced by the nondisclosure of their names and the other information requested.

JEROME L. GETZ
Special Assistant
Attorney General

Subscribed and sworn to before me this 24th day of October, 1986. Kim J. Wagner, Notary Public.

APPENDIX F

STATE OF MINNESOTA
OFFICE OF ADMINISTRATIVE HEARINGS

FOR THE MINNESOTA
DEPARTMENT OF COMMERCE

COM/S-86-047-JL
8-1005-698-2

In the Matter of CAUCUS DISTRIBUTORS, INC., and CAMPAIGNER PUBLICATIONS, INC., New York Corporations, INDEPENDENT DEMOCRATS FOR LaROUCHE, an unincorporated association, RON FREDMAN, RONALD R. BETTAG, PAUL GREENBERG, and all other persons and organizations acting in concert with the named respondents.

ORDER DENYING MOTION FOR PRECLUSION, ESTABLISHING REPORTING REQUIREMENTS AND SETTING A HEARING DATE

The above-entitled matter is pending before the undersigned Administrative Law Judge pursuant to hearing orders issued by the Commissioner of Commerce. Patrick J. Moran, Moran & Pilger, P.A., Attorneys at Law, 1221 Lamar, Suite 517, Houston, Texas 77010, has appeared on behalf of the above-named Respondents. Jerome L. Getz, Special Assistant Attorney General, 1100 Bremer Tower, Seventh Place and Minnesota Street, St. Paul, Minnesota 55101, has appeared on behalf of the Minnesota Department of Commerce (Department).

On October 27, 1986, the Department filed a Motion for an order precluding the Respondents from contesting the allegations in the Amended Cease and Desist Order or raising any affirmative defenses to those allegations, or in the alternative, an order that any allegations in the Amended Cease and Desist Order that the Department might be able to prove by the testimony of the persons whose names were to be disclosed pursuant to the Judge's Discovery Order of October 6, 1986, be deemed admitted and that the Respondents be precluded from raising any affirmative defenses which might be rebutted by the testimony of those persons. On October 28, 1986, commencing at 10:00 a.m., a telephone conference was held between the parties and the Judge to discuss the Department's Motion and the Respondents' objections to it. Pursuant to the Judge's directive, the Respondents have provided affidavits regarding their inability to comply with prior discovery orders and have filed a status report.

Based upon all the files, records and proceedings herein, including the arguments and affidavits submitted by the parties,

IT IS HEREBY ORDERED:

1. That the Department's request for preclusion or other sanctions as a result of the Respondents' failure to comply with discovery orders is DENIED.

2. That a prehearing telephone conference will be held between the parties and the Judge at 1:00 p.m. on Friday, December 12, 1986, to discuss the Respondents' request that persons who desire anonymity be exempted from the Judge's Discovery Order and to discuss the status of the Respondents' efforts to comply with paragraph 4 of this Order.

3. That the hearing will reconvene, assuming compliance with the Judge's discovery orders, on Wednesday, January 28,

1987, at 9:00 a.m. at the Office of Administrative Hearings. Three days have been scheduled for its completion.

4. That the Respondents shall immediately take reasonable steps to obtain a list of the persons to whom loans have been made from the personal recollections of Ron Fredman, Ronald R. Bettag and Paul Greenberg, and from the records that do exist in the Respondents' Chicago offices, and be prepared to discuss the efforts that it has undertaken during the telephone conference on December 12.

Dated this 2nd day of December, 1986.

JON L. LUNDE
Administrative Law Judge

MEMORANDUM

In response to the Department's request for the imposition of sanctions against the Respondents for their failure to provide a list of names of Minnesota lenders and the documents pertaining to the loans that were made, the Respondents have submitted two affidavits of Suzanne Rose. In her affidavits, Ms. Rose stated that the Respondents have been unable to fully comply with the discovery orders issued in this case because its business records were seized by federal and state authorities on October 6, 1986, pursuant to a search warrant issued to the Attorney General of the State of Virginia. Among the documents seized at that time were a list of Minnesota lenders and contributors and the documents underlying those transactions.

In determining whether sanctions should be imposed for noncompliance with a discovery order, the Judge must consider the following factors:

(1) Prejudice to the party seeking discovery,

(2) Whether the noncomplying party had clear warning that noncompliance would result in the imposition of sanctions,

(3) Whether less harsh sanctions can accomplish the objectives of securing discovery compliance while assuring that the parties are properly prepared for trial, and

(4) The willfulness of the party's noncompliance.

See, e.g., Dennie v. Metropolitan Medical Center, 387 N.W.2d 401 (Minn. 1986); *Hoyland v. Kelly*, 379 N.W.2d 150 (Minn. App. 1985).

In this case, the Respondents had clear warning that noncompliance would result in the imposition of sanctions. Notice was given to the Respondents during telephone conferences with the Department and the Judge, and notice was included in one of the Judge's prehearing orders. In addition, less severe alternatives to the imposition of sanctions are not available, due largely to the fact that the Judge is not authorized, in this proceeding, to tax any costs or disbursements against the Respondents. Nonetheless, the imposition of sanctions in this case is inappropriate because the delays that will be occasioned by the Respondents' noncompliance are not significantly prejudicial to the Department and because the Respondents' noncompliance was due, in a large part, to its inability to comply due to the seizure of its business records. Therefore, the Judge is not persuaded that the imposition of sanctions is appropriate at this time.

J.L.L.

APPENDIX G

STATE OF MINNESOTA
OFFICE OF ADMINISTRATIVE HEARINGS

FOR THE MINNESOTA DEPARTMENT
OF COMMERCE

COM/S-86-047-JL
8-1005-698-2

In the Matter of CAUCUS DISTRIBUTORS, INC., and CAMPAIGNER PUBLICATIONS, INC., New York Corporations, INDEPENDENT DEMOCRATS FOR LaROUCHE, an unincorporated association, RON FREDMAN, RONALD R. BETTAG, PAUL GREENBERG, and all other persons and organizations acting in concert with the named respondents.

DISCOVERY ORDER

On Friday, December 12, 1986, a prehearing telephone conference was held between the undersigned Administrative Law Judge and counsel for both parties to this case. The purpose of that telephone conference was to discuss the Respondents' efforts to comply with prior discovery Orders and to determine whether the Judge's prior discovery Orders should be modified to recognize that certain individuals have requested that their names not be disclosed to the Department.

Based upon the determinations made during the prehearing telephone conference on December 12, 1986,

IT IS HEREBY ORDERED:

1. That on or before December 19, 1986, the Respondents shall mail to the Department's counsel a list of the names and addresses of all persons residing in, or whose mailing addresses are located within, the State of Minnesota to whom offers or sales of promissory notes or other securities have been made; the dates of said offers or sales, the amounts thereof, the type or types of promissory notes or other securities involved, if there are more than one, and the name of the person making such offer or sale; and all writings of every kind and description, including handwritten notes, in the possession of Respondents concerning loans made by such persons during the period from September 1, 1983, to April 30, 1986, provided, however, that the Respondents need not disclose the names of any individuals or other information pertaining to the loans made by individuals that have requested anonymity under this paragraph.

2. If the Respondents are unable to provide all the writings specified in paragraph 1 on December 19, 1986, the Respondents shall notify the Department's counsel of the documents that have not been disclosed, the reasons for nondisclosure, and the date by which they will be provided.

3. On December 19, 1986, the Respondents shall also submit to the Judge, under seal, the information specified in paragraph 1 for those individuals who have requested anonymity. The Judge will randomly select 25 percent of the names of those individuals and accompanying data and provide it to the Department's counsel. At the same time, the Judge will notify the Respondents of the names randomly selected. Upon receipt of that notification, the Respondents shall forthwith provide Department's counsel with the information specified in paragraph 2 regarding those individuals.

4. All information provided to the Department pursuant to this Order is subject to the same protective Order contained in the Judge's October 6, 1986 Discovery Order.

5. Noncompliance with this Order shall result in the imposition of sanctions, including the issuance of a default determination, striking certain defenses, or precluding the presentation of evidence.

Dated this 15th day of December, 1986.

JON L. LUNDE
Administrative Law Judge

APPENDIX H

STATE OF MINNESOTA
OFFICE OF ADMINISTRATIVE HEARINGS

FOR THE MINNESOTA DEPARTMENT OF COMMERCE

COM/S-86-047-JL
8-1005-698-2

In the Matter of CAUCUS DISTRIBUTORS, INC., and CAMPAIGNER PUBLICATIONS, INC., New York Corporations, INDEPENDENT DEMOCRATS FOR LaROUCHE, an unincorporated association, RON FREDMAN, RONALD R. BETTAG, PAUL GREENBERG, and all other persons and organizations acting in concert with the named respondents.

ORDER DENYING CERTIFICATION AND A STAY

On December 15, 1986, a Discovery Order requiring the Respondents to disclose information concerning loans made to them by Minnesota residents was issued. The terms of that Discovery Order repeated verbal determinations made by the Administrative Law Judge during a telephone conference with counsel on December 12, 1986. Subsequently, after the time for compliance with the Discovery Order expired, Respondents notified the Administrative Law Judge that they would not comply with it. In their letter, the Respondents requested an opportunity for an interlocutory appeal of the Discovery

Order or a stay which would permit them to litigate that Order in Federal Court. On December 29, 1986, counsel were notified, by letter, that the Respondents' December 23, 1986 letter would be treated as a Motion for a stay in the imposition of sanctions pending court action to challenge the Discovery Order issued, and advising the Department that it should respond to it as a Motion. On January 12, 1987, the Department filed its objections to the relief requested by the Respondents.

Based upon all the files, records and proceedings herein,

IT IS HEREBY ORDERED:

1. That the Respondents' requested interlocutory appeal of the Discovery Order in this case is DENIED.

2. That the Respondents' requested stay of the scheduled hearing is DENIED.

3. That in the absence of a Court Order to the contrary, the hearing will proceed as scheduled on January 28, 1987.

4. That in the absence of a Court Order modifying the Discovery Order, sanctions for noncompliance with it will be imposed.

5. That no sanctions will be imposed until the Respondents have an opportunity to submit written arguments addressing the propriety of the sanctions proposed by the Department in the Memorandum it filed with the Administrative Law Judge on January 12, 1987.

6. That the Respondents shall reply to the sanctions proposed by the Department in writing on or before January 26, 1987.

Dated this 13th day of January, 1987.

JON L. LUNDE
Administrative Law Judge

MEMORANDUM

Under Minn. Rule 1400.7600 (1985), some Motions may be certified to an agency. The rule permits certification before or after the issuance of an Order. The rule states in part:

> * * * Any party may request that a pending motion or a motion decided adversely to that party by the judge before or during the course of the hearing, other than rulings on the admissibility of evidence or interpretations of parts 1400.5100 to 1400.8400, be certified by the judge to the agency. * * *

Under the rule cited above, discovery orders and motions for discovery are not certifiable because they involve interpretations of the discovery rules of this office. Consequently, Respondents' request for an interlocutory appeal of the disputed Discovery Order may not be granted. Since the Judge has no other source of authority for granting an interlocutory appeal to a party, its first request must be denied.

The Administrative Law Judge does have authority to continue the date of the hearing under Minn. Rule 1400.7500 (1985) upon a showing of good cause. However, the Administrative Law Judge is not persuaded that good cause exists to stay the scheduled hearing. Several delays have already occurred and the Administrative Law Judge has no guarantees that the Respondents will, in fact, seek or obtain interlocutory review of the disputed Discovery Order or that interlocutory relief will be diligently pursued. Under the circumstances, the requested stay should be denied.

If the Respondents desire interlocutory review, they should seek relief in the appropriate court and obtain the necessary writ of prohibition or a temporary injunction restraining this proceeding. Any other disposition would permit the Respondents to unnecessarily prolong this proceeding and deprive the

Department and the Judge of any control over the prompt filing and diligent prosecution of the relief it seeks.

Before sanctions are imposed, Respondents should be given an opportunity to respond to the specific sanctions suggested by the Department in its Memorandum of January 9, 1987. Delaying the imposition of sanctions will also enable the Respondents to seek judicial relief before any sanctions are imposed.

J.L.L.

APPENDIX I

STATE OF MINNESOTA
OFFICE OF ADMINISTRATIVE HEARINGS

FOR THE MINNESOTA DEPARTMENT
OF COMMERCE

COM/S-86-047-JL
8-1005-698-2

In the Matter of CAUCUS DISTRIBUTORS, INC., and CAMPAIGNER PUBLICATIONS, INC., New York Corporations, INDEPENDENT DEMOCRATS FOR LaROUCHE, an unincorporated association, RON FREDMAN, RONALD R. BETTAG, PAUL GREENBERG, and all other persons and organizations acting in concert with the named respondents.

ORDER IMPOSING SANCTIONS
FOR NONCOMPLIANCE
WITH DISCOVERY

On October 6, 1986, a Discovery Order requiring the Respondents to disclose information concerning loans to them by Minnesota residents was issued. The Respondents did not comply with the terms of that Discovery Order. Consequently, on October 27, 1986, the Minnesota Department of Commerce (Department) moved for an Order precluding the Respondents from contesting the allegations in the Amended Cease and Desist Order or raising any affirmative defenses to the allegations set forth therein. On October 28, 1986, a telephone

conference was held to discuss the Department's Motion and the Respondents' objections to it. On December 2, 1986, an Order was issued denying the Department's request for the imposition of sanctions, ordering the Respondents to take reasonable steps to comply with the October 6 Discovery Order, and scheduling a telephone conference for December 12, 1986. On December 15, 1986, an additional Order was issued which required the Respondents to disclose information concerning loans made to them by Minnesota residents. That Discovery Order repeated verbal determinations made by the Administrative Law Judge during a telephone conference with counsel on December 12. After the time for compliance with the December 15, 1986 Discovery Order expired, Respondents notified the Judge that they would not comply with it. In their letter, the Respondents requested an opportunity for an interlocutory appeal of the Discovery Order or a stay which would permit them to litigate that Order in court. On January 12, 1987, the Department filed its objections to the relief requested by the Respondents. On January 13, 1987, the Respondents' request for certification of the Judge's Discovery Order or a stay pending a challenge of that Order was denied. At the same time, the Respondent was ordered to respond to the Department's Motion for the imposition of sanctions for noncompliance with the Judge's Discovery Orders. On Monday, January 26, 1987, the Respondent filed its objections to the imposition of sanctions.

NOW, THEREFORE, based upon the files, records and proceedings herein,

IT IS HEREBY ORDERED: That pursuant to the provisions of Minn. Rule 1400.6700, subp. 3 (1985), the Respondents are hereby precluded from contesting the last sentence in paragraph 1, and paragraphs 2 and 7 of the Department's

Amended Cease and Desist Order due to their expressed intention not to comply with the Judge's December 15, 1986 Discovery Order.

Dated this 27th day of January, 1987.

JON L. LUNDE

Administrative Law Judge

MEMORANDUM

On December 24, 1986, counsel for the Respondents notified the Administrative Law Judge in writing that the Respondents would not comply with the December 15, 1986 Discovery Order requiring them to disclose the names of some of the Minnesota residents who made loans to them. The Respondents' failure to comply with that Discovery Order makes it virtually impossible to determine the legal issues raised in the Department's pleadings or whether the Department's Cease and Desist Order should be made permanent. Since the information requested by the Department is essential in order to properly administer the securities laws of this State or to determine whether the promissory notes issued by the Respondents constitute securities, the Department will be substantially prejudiced by the Respondents' noncompliance. Since the Respondents have had clear warning that sanctions would be imposed for noncompliance, since their refusal to comply is willful, since they have not challenged the Order in Court, and since less severe alternatives are not available, severe sanctions should be imposed. *See, e.g., Sudheimer v. Sudheimer*, 372 N.W.2d 792 (Minn. App. 1985); *Peters v. Peters*, 374 N.W.2d 335 (Minn. App. 1985); *Hoyland v. Kelly*, 379 N.W.2d 150 (Minn. App. 1985). *See also, First National Bank of Shakopee v. Department of Commerce*, 310 Minn. 127, 245 N.W.2d 861 (1976).

The Respondents argue that the information the Department now has is sufficient and that no sanctions should be imposed before they have an opportunity to challenge the Discovery Order in Court. Neither of those arguments are persuasive. In determining whether the Respondents have sold securities in the State of Minnesota, a substantial number of diverse factors and transactions must be examined. The Administrative Law Judge is not persuaded that the Department has been provided with enough information to make a reliable or adequate record in this case. In addition, the Judge is not persuaded that sanctions should be postponed until the constitutional issues raised by the Respondents are decided in Court. If the Respondents wanted to challenge that Order in Court, they should have done so long ago. Withholding sanctions until the Respondents seek and obtain review of the Discovery Order could result in an indefinite delay in the resolution of the issues in this case. That should not happen based on the Respondents' mere allegation that it will seek and obtain Court review at some unspecified time.

J.L.L.